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No. OFFICE OF THE CLERK

IN THE

Supreme Court of the United States

OCTOBER TERM, 1997

FIGTER LIMITED,

Petitioner,

vs.

TEACHERS INSURANCE AND ANNUITY ASSOCIATION OF AMERICA,

Respondent.

ON PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

PETITION FOR WRIT OF CERTIORARI

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QUESTIONS PRESENTED FOR REVIEW

1. Under the circumstances presented in this case, should various unsecured claims purchased by a fully secured creditor in a case under Chapter 11 of the Bankruptcy Code (the "Code"), 11 U.S.C. § 1101 *et seq.*, be determined as being not in good faith and designated as nonvoting under Section 1126(e) of the Code, where such purchases were made for the admitted purpose of blocking confirmation of the Chapter 11 debtor's proposed plan of reorganization, by depriving the debtor of utilizing the unsecured creditor class as the requisite consenting, impaired class needed to obtain confirmation of such plan, thereby jeopardizing such debtor's prospects for a successful reorganization and a fresh start?

2. Under the circumstances presented in this case, if the unsecured claims purchased by such fully secured creditor are not designated as nonvoting under Section 1126(e) of the Code, should the claims purchased be deemed to be a single claim for the purpose of voting on the debtor's proposed Chapter 11 plan of reorganization?

3. Should the Court of Appeals have reviewed the decisions of the courts below on the issue of determining good faith entirely *de novo*, either as issues of law or as mixed issues of law and fact, instead of under a clearly erroneous standard?

LIST OF PARTIES TO THE PROCEEDING

Petitioner Figter Limited ("Figter") is a California limited partnership. Petitioner Figter's sole general partner is Geoff Palmer, a California resident, who, as a general partner, is a 90% equity interest holder in Figter. Figter's sole limited partner is Dan Saxon Palmer, a California resident and the brother of Geoff Palmer, who is a 10% equity interest holder in Figter.

Respondent Teachers Insurance and Annuity Association of America ("TIAA") is a nonprofit Internal Revenue Code Section 503(c)(3) New York corporation whose shares have been issued to the TIAA Board of Trustees. To the best knowledge of petitioner Figter, TIAA has no parent companies or nonwholly owned subsidiaries.

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OPINIONS BELOW

The order and memorandum of decision by the United States Bankruptcy Court for the Central District of California (the "Bankruptcy Court") in *In re Figter Limited*, Case No. SV 93-29168-AG (Bankr. C.D.Cal.) was entered May 3, 1995 and is unreported (the "Bankruptcy Court Order") (App. C herein). The Order Affirming Decision of Bankruptcy Court by the United States District Court for the Central District of California (the "District Court"), Case No. CV 95-4462-SVW (C.D.Cal.) was entered January 29, 1996 and is unreported (the "District Court Order") (App. B herein). The Opinion of the United States Court of Appeals for the Ninth Circuit affirming the District Court Order was entered on June 24, 1997 and is reported at 118 F.3d 635 (the "Ninth Circuit Opinion") (App. A herein).

JURISDICTION

The judgment of the Court of Appeals (App. A herein) was entered on June 24, 1997. The jurisdiction of this Court is invoked pursuant to 28 U.S.C. § 1254(1).

STATUTORY PROVISIONS INVOLVED

The pertinent text of the following statutory provisions is set forth in Appendix D:

Bankruptcy Code Section 1126, 11 U.S.C. § 1126;

Bankruptcy Code Section 1129, 11 U.S.C. § 1129.

STATEMENT OF THE CASE

This appeal arises in the context of the Chapter 11 bankruptcy case of petitioner Figter and from the purchases by respondent TIAA of twenty-one claims in the unsecured

creditor class in which it was previously not a member. It is undisputed that TIAA's purpose in purchasing the unsecured claims was to block Figter's then proposed plan of reorganization. The Court of Appeals affirmed the determinations of the Bankruptcy Court and the District Court below that the purchased claims would not be designated as having been purchased in bad faith and that TIAA could cast one vote for each of the purchased claims. Figter seeks review by this Court of these holdings because they were decided erroneously, because of their serious and adverse impact not only on Figter's ability, but on the ability of other Chapter 11 debtors, to reorganize and otherwise to seek the protections of the Code in the manner which Congress intended, because of their adverse affect on the function and operation of the Code in contravention of Congressional intent with respect thereto, and because they contravene holdings of this Court with respect to the role of the Federal courts in the Chapter 11 reorganization process.

Figter commenced its case under Chapter 11 of the Code by the filing of a voluntary petition in the Bankruptcy Court on May 27, 1993. Figter's primary asset is a 198-unit multifamily residential complex ("Skyline Terrace") located in downtown Los Angeles, California. The Bankruptcy Court exercised jurisdiction pursuant to a referral of jurisdiction under 28 U.S.C. § 157. The District Court's subject matter jurisdiction was based on 28 U.S.C. §§ 158(a) and 1334.

Applicable Provisions of the Code.

Under the Code, in order to obtain confirmation of a plan of reorganization, the proponent of the plan (here, petitioner Figter) must satisfy each of the requirements set forth in Section 1129(a) of the Code. Among other requirements, Section 1129(a)(8) requires that every class of claims which are impaired under the plan (*i.e.*, have statutory, contractual or other rights altered under the plan) must have voted to

accept the plan and Section 1129(a)(10) requires that at least one impaired class of creditors must have accepted the plan. Section 1129(b) (the so-called "cramdown" provision of the Code) provides that, if all the requirements of Section 1129(a) are met, except for Section 1129(a)(8) (acceptance by all impaired classes), a plan may still be confirmed, provided the "cramdown" provisions set forth in Section 1129(b) are met.

Section 1126(c) provides that a class of claims has "accepted" a plan if such plan has been voted to be accepted by creditors, other than a creditor "designated" under Section 1126(e) of the Code, that hold at least two-thirds in amount *and* more than one-half in number of the allowed claims in such class held by creditors, other than a creditor "designated" under Section 1126(e), that have actually voted to accept or reject the plan. Thus, a creditor may seek to obtain a "blocking position" to prevent the acceptance of a plan by a class by purchasing *either* at least two-thirds in amount *or* more than one half in number of the claims in such class. In a situation where, as here, there were essentially only two impaired classes of creditors, a creditor which is the sole or controlling creditor in one impaired class, as here, may seek to prevent confirmation of a plan by purchasing the requisite amount of claims in the other class so as to preclude the debtor from meeting the requirement of Section 1129 (a) (10) that at least one impaired class of claims must accept the plan.

Section 1126(e) provides that, after notice and hearing, a Bankruptcy Court may "designate" any entity whose acceptance or rejection of a plan "was not in good faith, or was not solicited or procured in good faith." Thus, as discussed below, if a creditor is found not to have acted in good faith, such as, for example, in connection with the purchase of claims, its claims may not be voted or counted in connection with confirmation of a plan.

In addition to the foregoing provisions, Section 1125 of the Code sets forth detailed provisions regarding disclosure and solicitation of creditors in connection with the Chapter 11 plan process. In brief, Section 1125(b) provides that acceptances or *rejections* of a proposed plan may not be solicited from any claim holders unless at the time of or before such solicitation there is transmitted to such holders the plan, or a summary thereof, and a disclosure statement approved, after notice and hearing, by the Bankruptcy Court as containing "adequate information." Section 1125(a)(1) defines "adequate information" as information of a kind, and in sufficient detail, that would enable a "hypothetical reasonable investor typical of holders of claims or interests of the relevant class to make an informed judgment regarding the plan."

Facts.

Figter filed its initial Plan of Reorganization (the "Plan") on December 23, 1993, and filed a proposed amended Disclosure Statement on November 14, 1994. TIAA filed a competing plan of reorganization and a proposed disclosure statement, which were not withdrawn until December 16, 1994. Essentially, the Plan provided for the apartment units of Skyline Terrace to be converted to condominiums and sold, thereby generating cash to pay unsecured and secured claims. Figter's sole secured creditor, classified by itself as Class 2 under the Plan, is TIAA. The Plan provided for the full payment, over time, of TIAA's claim (which consists of a loan in the principal amount of approximately $15 million, with interest at 9 percent per annum, secured by a lien on Skyline Terrace), together with a market rate of interest. The Plan also provided that Class 3 under the Plan (Figter's general unsecured creditors) would be paid 80% of the face amount of such creditors' allowed claims. Class 2 and 3 were the only impaired classes under the Plan.

Figter also had commenced a lender liability action as an adversary proceeding in the bankruptcy case on or about December 14, 1993 (the "Adversary Proceeding"). In the Adversary Proceeding, Figter claims that, among other things, TIAA is liable to Figter arising out of TIAA's efforts to foreclose upon Skyline Terrace at all costs, by all means necessary and in bad faith, thereby depriving Figter of its substantial equity in Skyline Terrace, to the detriment of Figter and its unsecured creditors.

The Bankruptcy Court has determined that, as of May 31, 1994, the value of Skyline Terrace was $19.3 million and that the indebtedness of TIAA was approximately $18 million. By virtue of its security interest in Figter's cash on hand, which was then in excess of $1.4 million, combined with its security interest in Skyline Terrace, TIAA's claim was determined by the Bankruptcy Court to be fully secured as of May 31, 1994. As a result of such findings, it was determined that TIAA was not an unsecured Class 3 creditor under the Plan.

Unknown at the time to Figter or the Bankruptcy Court, from on or about October 27, 1994 and continuing through October 31, 1994, TIAA purchased 21 of the unsecured claims in this case at 100% face value, for a total of $14,588.62. Such purchases were made prior to any disclosure statement having been transmitted to any of Figter's creditors. The purchases constituted over 50% in number of Figter's general unsecured claims, which meant that the Plan could not be accepted by Figter's Class 3 general unsecured creditors as then constituted. In light of TIAA's opposition to the Plan, Figter would not have been able to have the Plan confirmed since no impaired class would have voted to accept it.

Proceedings Below.

On February 7, 1995, TIAA filed its motion in the Bankruptcy Court for an order declaring that its purchases of unsecured claims was in good faith under Section 1126(e) of the Code. On February 16, 1995, Figter filed a cross-motion, pursuant to Sections 105 and 1126(e) of the Code, to designate the claims purchased by TIAA as nonvoting on the grounds that such claims were purchased by TIAA in bad faith, and, if the Bankruptcy Court declined to designate the claims, to have the Bankruptcy Court declare that TIAA would have only one vote in Class 3 and not 21 separate votes by virtue of its claims purchases.

In the Bankruptcy Court Order, the Bankruptcy Court found that TIAA's claims purchases were in good faith and that TIAA was entitled to one vote for each claim purchased. The District Court affirmed the Bankruptcy Court Order. The District Court heard and decided the appeal of the Bankruptcy Court Order pursuant to 28 U.S.C. § 158(a). The District Court Order was affirmed by the Ninth Circuit Opinion entered on June 24, 1997. This petition for a writ of certiorari is being filed within 90 days of entry of the judgment of the Court of Appeals.

REASONS FOR GRANTING THE WRIT

Conflict with Supreme Court Precedent.

The primary purpose of Chapter 11 proceedings is to promote the successful reorganization of the debtor. Some of the stated purposes of the Code have been described as follows: "to provide debtor relief, facilitate feasible reorganizations, preserve equality among similarly situated creditors, and assure equitable loss distribution." L. Rusch, "Single Asset Cases and Chapter 11: The Classification Quandary," 1 Am. Bankr. Inst. L. Rev. 43, 58-59 (Spring

1993). It is the Bankruptcy Court's role, within the bounds of the law, to further the primary goal of debtor reorganization in a Chapter 11 case. *Pioneer Investment Services Co. v. Brunswick Assoc. LP*, 507 U.S. 380, 389 (1993) ("... bankruptcy courts are entrusted with broad equitable powers to balance the interests of the affected parties, *guided by the overriding goal of insuring the success of the reorganization*"; emphasis added).

With particular regard to the issue of bad faith raised by respondent TIAA's claims purchases, this Court in *Young v. Higbee*, 324 U.S. 204, 210-211 (1945), stated that the purpose of the predecessor statute to Section 1126(e) of the Code was as follows:

> The history of this provision [Section 203 of the Bankruptcy Act of 1898, 11 U.S.C. § 603] makes clear that it was intended to apply to those stock holders whose selfish purpose *was to obstruct a fair and feasible reorganization* in the hope that some one would pay them more than the ratable equivalent of their proportionate part of the bankrupt assets.

324 U.S. at 211 (emphasis added). In interpreting Section 1126(e) of the Code, the Ninth Circuit Opinion was clearly not guided by the *overriding goal* of insuring the success of the reorganization. To the contrary, the Ninth Circuit Opinion interpreted the statute in a manner which renders it difficult, if not impossible, for Figter to reorganize. Furthermore, the Ninth Circuit Opinion refused to apply the holding of this Court's decision in *Young v. Higbee, supra*, that a selfish purpose to *obstruct a fair and feasible reorganization* constitutes bad faith, resulting in denial of the right to vote on a plan. Respondent TIAA admitted that the purpose of its claims purchases was to block confirmation of the Plan and, if this Court's precedent had been followed and applied by the Court of Appeals, a finding of bad faith should have been made.

The Ninth Circuit Opinion is also in conflict with precedents of this Court on the issue of whether respondent TIAA, if the claims it purchased are not designated as non-voting, should have been found entitled to only one vote with respect to the claims it purchased. As discussed below, in a variety of pre-Code contexts, the assignee or holder of multiple claims in the same class has only one vote for purposes of voting in a bankruptcy proceeding. In *Dewsnup v. Timm*, 502 U.S. 410, 419-420 (1992), this Court held that, unless there is a discussion to the contrary in the legislative history, the Code is not to be construed as intending "to effect a major change in pre-Code practice." Contrary to the holding of this Court, the Court of Appeals embarked upon a "major change in pre-Code practice," by rejecting analogous bankruptcy precedent decided in a variety of analogous contexts, and in the context of the predecessor statutes to Chapter 11 of the Code, without even the slightest reference to any legislative history which might justify such a departure.

Adverse Affect and Impact on the Code and its Purposes.

The impact of the Ninth Circuit Opinion would not be limited to the particular facts of this case. Its impact would be seen in a variety of circumstances, involving any Chapter 11 debtor and a secured creditor or creditors in such a case. If not reversed, the Ninth Circuit Opinion would permit any secured creditor in a Chapter 11 case to launch a surreptitious pre-emptive strike to purchase a blocking position so as to prevent a Chapter 11 debtor from meeting the requirements of Section 1129 and thereby to have a plan of reorganization confirmed. The consequence of the Ninth Circuit Opinion would thus severely undermine the operation and purposes of the Code. If the Federal courts were to sanction the activity at issue by a secured creditor, it would have the

practical and adverse affect of preventing any reorganization in a Chapter 11 case where the secured creditor decided to engage in such tactics. Indeed, the Ninth Circuit Opinion has already been cited by one Bankruptcy Court in refusing to designate the unsecured claims purchased by a creditor as nonvoting under Section 1126(e). *In re Crosscreek Apartments*, 1997 Bankr. LEXIS 1304 (Bankr. E.D. Tenn. Aug. 19, 1997).

The Ninth Circuit Opinion will result in a "free for all" whereby a secured creditor will attempt, as in the case at bar, to buy as many claims as possible to obtain a blocking position *before* any plan has been proposed so that creditors will know how they will be treated by the debtor in such plan and *before* any Court-approved disclosure statement has been transmitted to creditors so that they have adequate information prior to determining whether to sell their claims, all in contravention of the disclosure and solicitation provisions of Section 1125 of the Code. By being able to buy claims without compliance with Section 1125, a secured creditor such as TIAA attains an enormous undue advantage over a Chapter 11 debtor, who is required to comply with Section 1125 before soliciting acceptances from creditors. In the meantime, a secured creditor will have acquired its blocking position without adhering to the strictures of Section 1125.

See, e.g., In re Applegate Property, Ltd., 133 B.R. 827 (Bankr. W.D. Tex. 1991) (votes of insiders disqualified who had purchased claims to prevent the proponent of a competing plan from purchasing them). The Court in that case stated as follows regarding all claims trading involving the purchase of a blocking position:

> Sanctioning claims acquisition for purposes of blocking an opponent's plan would also ignite a scramble for votes conducted almost entirely outside the Code's carefully developed structure (plan, disclosure statement, equal treatment, regulated solicitation, court-supervised confirmation),

> leaving creditors to select not the best plan but the best deal they might be able to negotiate. Creditors would be paid, no doubt, but not equally, and not on the basis of accurate information. Such a wild free-for-all may appeal to the entrepreneurial capitalist, but it also issues a gilt-edged invitation to fraudulent and corrupt practices, to say nothing of the ramifications of buying claims in exchange for forbearance, a potential violation under the federal securities laws.

133 B.R. at 836.

To allow, as the Ninth Circuit Opinion does, a secured creditor to trade in claims in the manner engaged in by TIAA would promote the kind of "free-for-all" outside the "Code's carefully developed structure" as set forth in Sections 1125 (providing for a Court-approved disclosure statement to be used in soliciting acceptances of a plan), 1126 (setting forth voting procedures on a plan) and 1129 (setting forth confirmation requirements) of the Code.

Therefore, the designation of the unsecured claims purchased by TIAA as nonvoting will preserve the primary purpose of Chapter 11 and prevent the type of abuse by creditors in Chapter 11 cases in which TIAA has engaged. Indeed, TIAA's tactic in purchasing claims to block confirmation of a debtor's plan is not and cannot be an isolated case. It has been estimated, for example, that in 1993, trading in bankruptcy claims totaled $13 billion. R. Kaufman, "Redress Distress by Trading the Debt; Activity in Secondary Market Increases," N.Y. L.J., October 12, 1993, at 11. It would be a rare debtor, however, which would have the continuing economic viability, resources and opportunity to seek review by this Court of the pernicious conduct engaged in here. The fact that such claims trading may result in blocking the successful reorganization of a debtor does not mean that such conduct and its adverse consequences to the

purposes and policies underlying the Code should be insulated from review by this Court.

Adverse Affect and Impact on Single Asset Cases.

Petitioner Figter's primary asset is Skyline Terrace and Figter may be characterized as a "single asset real estate" debtor. As discussed above, the Ninth Circuit Opinion adversely affects all Chapter 11 cases. Single asset debtors, however, are particularly susceptible and vulnerable to a secured creditor engaging in the same tactics employed by respondent TIAA because such debtors typically have only one single secured creditor and a number of unsecured trade creditors. The sole secured creditor in such a situation may more easily acquire a blocking position to make it difficult, if not impossible, for the debtor to obtain the consent of at least one impaired class for plan confirmation purposes.

This adverse impact on single asset debtors also warrants review of the Ninth Circuit Opinion by this Court. The Code was most recently amended by Congress in 1994. Among other things, the 1994 amendments, Pub. L. 103-94, 108 Stat. 4106 (1994), added a definition of "single asset real estate" to the Code (in a new Section 51B) and set deadlines for the filing of proposed plans of reorganization and expiration of the automatic stay provisions of Section 362 of the Code for such "single asset real estate debtors." (Such amendments are not applicable to Figter since it filed its petition prior to the enactment of the 1994 amendments and since its secured debt exceeds the statutory maximum of $4 million). Significantly, as noted by some commentators, the 1994 amendments did *not* bar single asset debtors from seeking federal bankruptcy protection. To the contrary, as one bankruptcy practitioner has written, "If the policy of the Bankruptcy

Code was to eliminate the safety net for the single asset entrepreneur, Congress could have done so by way of the 1994 amendments by simply excluding this type of endeavor from the right to reorganize pursuant to chapter 11." D. Ravin, "Suggestion for the National Bankruptcy Review Commission and Congress," 4 Am. Bankr. Inst. L. Rev. 542 (Winter 1996). As another commentator has stated, "Indeed, if the statute [Chapter 11 of the Code] is relevant at all, one can make a respectable, if not conclusive, case that the drafters *intended* the bankruptcy process to accommodate the one asset case." J. Ayer, "Bankruptcy as an Essentially Contested Concept: The Case of the One-Asset Case," 44 S.C. L. Rev. 863, 872 (1993) (emphasis added). Accordingly, judicial interpretations of the Code, such as set forth in the Ninth Circuit Opinion, which render it difficult or impossible for a single asset real estate debtor such as Figter to reorganize, are inconsistent with the purpose and policy of the Code and the intent of Congress.

Under the totality of the circumstances in this case, TIAA did not act with proper motive or in a proper manner in purchasing the unsecured claims in question and otherwise acted in bad faith. In finding otherwise, the Court of Appeals and the courts below have ignored the dictates of this Court that they must have as an *overriding* goal, insuring the success of the reorganization. The decisions below jeopardizes the successful reorganization of Figter and is contrary to the teachings of this Court, the purposes of the Code and the intent of Congress. The petition should be granted so that the Court may exercise its supervisory power to correct this departure from applicable precedent and legislative intent.

Issues Presented.

The facts in this case are not in dispute. The Ninth Circuit Opinion is wrong as a matter of law, warranting review by this Court. This case presents the issue of whether the Court of Appeals erred in finding that unsecured claims purchased by a fully secured creditor in a Chapter 11 bankruptcy case should not be designated as nonvoting and as having been purchased in bad faith pursuant to Section 1126(e), where the following circumstances, among others, existed: (1) the sole secured creditor (TIAA) purchased the unsecured claims subsequent to having been determined to be fully secured in the case, and without previously having been a member of the unsecured creditor class; (2) the debtor and the secured creditor were involved in continuing litigation wherein, in essence, the debtor made allegations of bad faith against the secured creditor, prior to the purchase of claims; (3) the secured creditor was a plan proponent at the time it made the purchases; and (4) the purchase of the claims was for the primary and admitted purpose of, among other improper purposes, preventing the debtor from obtaining the confirmation of a plan of reorganization which had been filed and proposed over one year earlier, by depriving the debtor of the possibility of the consenting, impaired class it requires in order to effectuate a cramdown against the sole secured creditor. The clear answer is and should be that the Court of Appeals erred in affirming the refusal of the courts below to designate the claims purchased as in bad faith under the circumstances.

In addition, TIAA had and continues to have an irreconcilable conflict of interest with Figter's unsecured creditors. As the sole and fully secured creditor, TIAA's interests are diametrically opposed to the interests of the unsecured creditors in this case. Given this inherent conflict of interest, the claims purchasing by TIAA was not proper and the effect of allowing such trading, without imposing a voting sanction,

would be to discriminate unfairly against nonselling creditors in favor of those selling their claims to TIAA. The conflict of interest, and the potential for abuse, is exacerbated by the fact that TIAA was, at the time, itself a plan proponent, owing duties of disclosure and fair dealing to the class of creditors whose claims it was purchasing.

The existence of the Adversary Proceeding at the time TIAA conducted its claims purchasing further demonstrates TIAA's bad faith as a matter of law. One of the improper purposes which TIAA had in purchasing the subject claims and thwarting Figter's reorganization is to deprive Figter of both the incentive and the financial capability of pursuing the Adversary Proceeding. Moreover, Figter's unsecured creditors will be among the beneficiaries of any judgment against TIAA in the Adversary Proceeding, and thus TIAA's purchases of claims from the unsecured class, of which it was not a member, exacerbates its conflict of interest with the unsecured creditors.

Cases which have dealt with the issue of claims purchases indicate that evidence of an "ulterior" purpose or motive, aside from the purchasing creditor's status or prior status as a creditor, will establish bad faith. However, none of the cases indicate that such an "ulterior" motive is absolutely necessary to a finding of bad faith. In this regard, none of these cases immunized the purchasing creditor from the consequences of acting in bad faith simply because, in so acting, it was also acting in its own best interest. If this were the case, then, by definition, bad faith would never be found because it may be presumed that, if a creditor goes to great lengths to purchase claims, it is always doing so to promote its own self-interest. The holding of the Ninth Circuit Opinion in this regard has created a per se rule of immunity: so long as a creditor acts in its own self-interest, it does not and cannot act in bad faith. Such a holding is directly contrary not only to Supreme Court precedent, but decisions by other Federal courts, including those by other Courts of Appeals,

on this issue. *See, e.g., In re P-R Holding Corp.*, 147 F.2d 895 (2d Cir. 1945) (purchases of certificates were in bad faith where the purchases resulted in discrimination in favor of selling creditors).

On the basis of the foregoing, and based on the following arguments, this Court should send a signal to fully secured creditors in Chapter 11 cases who decide to engage in the kind of tactics engaged in by TIAA in this case. In so doing, the Court need not create and will not be creating new law. Such a ruling would be consistent with the jurisprudence of this Court interpreting the purposes of bankruptcy proceedings generally and, specifically, Chapter 11 proceedings. Such a ruling would also be consistent with bankruptcy court cases such as *In re Allegheny International*, 118 B.R. 282 (Bankr. W.D.Pa. 1990), which does not allow parties to unduly and in bad faith obstruct the reorganization process, even in advancing their own self-interests.

This case also presents the issue of whether the courts below erred in holding that the claims purchased by TIAA should not be designated as only *one* claim for purposes of voting. The rulings below are in contravention of a long line of jurisprudence, in various analogous pre-Code bankruptcy contexts, which hold that the holder of multiple claims only has one vote, even in the absence of bad faith, and Supreme Court case law holding that the Code was not intended to effect a major change in pre-Code practices absent some discussion in the legislative history to the contrary.

The Ninth Circuit Opinion Ignored or Did Not Apply Applicable Precedent as to "Good Faith" Under Section 1126(e).

Section 1126(e) is derived from Section 203 of the Bankruptcy Act of 1898 (the "Act," the Code's predecessor), 11 U.S.C. § 603. *See* 6 A. Herzog and L. King, *Collier Bankruptcy Practice Guide*, Section 94.10(4) at 94-113 (1994

ed.) ("*Collier's*"). *See also In re Allegheny, supra*, 118 B.R. at 287-288 (holding that cases decided under Section 203 of the Act are good authority under Section 1126(e)). Section 203 *explicitly* referred to trading in claims as a ground for finding bad faith.[1]

The rationale for the Act's good faith requirement was articulated in *Young v. Higbee, supra*, 324 U.S. at 210-211, as being designed to prevent the use of obstructionist and hold-up tactics by creditors in an effort to extract advantage for themselves from the debtor, or to gain preferential treatment, such as control of the debtor in exchange for their vote. This Court found that the legislative history of Section 203 relating to disqualifying the vote of a claimant or stockholder where it was not in good faith was expressly meant to overrule such holdings as *Texas Hotel Securities Corp. v. Waco Development Co.*, 87 F.2d 395 (5th Cir. 1936), *cert. denied sub nom. Waco Development Co. v. Rupe*, 300 U.S. 679 (1937).

The Court in *Allegheny, supra*, held that the acquisition of a blocking position by the purchasing party, Japonica, was in bad faith because it was aimed at defeating the debtor's plan and was meant to obstruct a fair and reasonable reorganization, citing *Young v. Higbee*. 118 B.R. at 289. The *Allegheny* court also found that Japonica, like Conrad Hilton in the *Waco* case (which was expressly overruled by Congress in Section 203 of the Act), bought a blocking position *after* the debtor proposed its plan of reorganization. *Id.* The Court in *Allegheny* took, in essence, a "totality of the circumstances" approach with regard to determining bad faith. Among other factors, the Court found that the following were

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[1] Section 203 of the Act provided: "If the acceptance or failure to accept a plan by the holder of any claim or stock is not in good faith, *in light of* or irrespective of *the time of acquisition* thereof, the judge may, after hearing upon notice, direct that such claim or stock be disqualified for the purpose of determining the requisite majority for the acceptance of the plan." (Emphasis added).

important in determining bad faith in that case: (1) the creditor did not purchase significant claims until the eleventh hour; (2) the creditor in the case had also been the proponent of a competing plan of reorganization; (3) the particular claims that the creditor purchased, and the manner in which they were purchased, indicated an intent to purchase a clear blocking position, insofar as a negative vote in the class in which the creditor purchased claims made confirmation extremely difficult, if not impossible; and (4) the amounts paid to purchase the claims indicated that the purchases were not made for economic purposes. 118 B.R. at 289-290. Thus, the Court found no valid economic reasons for the purchasing of the claims and found, instead, that the intent in purchasing claims was for the bad faith purpose of giving Japonica "unique control over the debtor and the process" through the purchase of a "blocking position." 118 B.R. at 289.

The rationale of Section 203 of the Act applies to the facts of this case. Here, TIAA is seeking to control and obstruct the confirmation process and to defeat the Plan, so that it can gain advantage for itself in the plan process and control the fate of Figter's sole real property asset, Skyline Terrace. The undisputed, admitted purpose of TIAA's purchases was to obtain a blocking position, insofar as a negative vote in the class in which TIAA purchased claims (Class 3 unsecured claims), as the Plan was then proposed, would have made confirmation extremely difficult, if not impossible, due to the lack of a consenting, impaired class to effectuate a cram-down. TIAA's purchases were clearly not made for economic purposes since it paid 100¢ on the dollar for claims for which, under the Plan, it would have received only 80¢. TIAA was clearly seeking "unique control over the debtor and the process" through the purchase of a blocking position to prevent the confirmation of the Plan.

Purchasing a blocking position to prevent confirmation of a plan, in and of itself, constitutes bad faith under Section

1126(e) due, in part, to the inherent possibility for abuse which claims trading involves. *E.g., Allegheny, supra*, 118 B.R. at 289; *In re Applegate Property, Ltd., supra*, 133 B.R. at 835 (votes of insiders disqualified who had purchased claims to prevent the proponent of a competing plan from purchasing them, because such conduct constituted an "obstructionist tactic done in contemplation of gaining an unfair advantage over other creditors" and because "such conduct cannot, as a matter of law, be in good faith").

To allow the purchase of a blocking position by a fully secured creditor, especially where it previously held no unsecured claim which it could argue it was trying to protect, would, in effect, sound the death knell for virtually all Chapter 11 cases. In every case, the secured creditor could simply purchase either 51% in number or over one-third in amount of the unsecured claims and thereby be virtually assured of being able to block the confirmation of a cramdown plan by the debtor. This cannot be the result which Congress contemplated when it enacted the Code. This is the very type of evil which Congress sought to empower and direct the bankruptcy courts to prevent when it enacted Section 1126(e) to address bad faith claims purchasing.

"Ulterior Motives" or "Improper Purposes" As Bad Faith.

As the Ninth Circuit Opinion acknowledged, cases have held that a vote must be designated where it is determined that the vote has been cast for an "ulterior purpose" and for purposes of gaining some advantage to which the creditor would not otherwise be entitled. The "ulterior" motive or special advantage may be one that is gained in the case itself and it need not be extrinsic or external to the bankruptcy case or to a plan in order to provide grounds for disqualification. Even though a secured creditor is entitled to vote in its own interests, and may even be allowed to acquire additional

secured claims in its own class to protect those interests, it is bad faith for the secured creditor to purchase claims outside its own class, from the class of unsecured creditors, in order to promote its interests as a secured creditor. Although cases such as *In re MacLeod Co.*, 63 B.R. 654, 655 (Bankr. S.D. Ohio 1986), have stated that bad faith under Section 1126(e) includes pure malice, strikes, blackmail and the purposeful destruction of a debtor's business, these are not, however, the exclusive circumstances where ulterior motives and bad faith may be found for purposes of Section 1126(e). In *In re Wiston XXIV, LP*, 153 B.R. 322, 326 (Bankr. D. Kan. 1993), for example, the Court designated the claims of a creditor who had entered into an agreement with a secured creditor to vote against the debtor's plan.

A creditor is also not immune, as the Ninth Circuit Opinion erroneously held, from having its vote disqualified as being in bad faith whenever it is acting in a bankruptcy case to protect what it argues as its best interests as a creditor. *E.g., In re Landing Associates, Ltd.*, 157 B.R. 791, 806 (Bankr. W.D. Tex. 1993) (no showing of "wrongdoing" by creditor for bad faith to be established, because this would be far too restrictive a test, and creditors can be held accountable where their conduct "tinges their participation in the equitable process with bad faith").

Contrary to the determination by the Court of Appeals, TIAA is not simply attempting to act in good faith to advance what it reasonably has determined to be its best interests as a creditor in this case. TIAA purchased claims *outside* the secured class to which TIAA belonged. TIAA *admitted* it purchased a blocking position in order to block the Plan's confirmation. In doing so, TIAA hoped to gain a preferential advantage over the other creditors. This is precisely the kind of behavior which this Court found constituted bad faith in *Young, supra*, 324 U.S. at 210-211. Furthermore, TIAA had an ulterior motive in purchasing the claims, which was to garner the equity in Skyline Terrace for

itself and hamper Figter's ability and incentive to continue the Adversary Proceeding.

The Court of Appeals also erroneously concluded that TIAA "reasonably" feared what would happen to its lien if the Plan were confirmed (App. A8). The undisputed evidence in the record is that, at all times, TIAA's claim was fully secured and adequately protected by an equity cushion. Further, the Debtor's condominium conversion plan is feasible and does not unduly transfer any risk to TIAA or any other creditors. The Bankruptcy Court has already found the essential elements of plan feasibility to exist when it determined the value of Skyline Terrace; namely, realistic sales prices, expense reductions and cash flow, absorption period and sales demand projections. TIAA would have a lien on the condominium units and common areas, which will be partially released as units are sold.

If respondent TIAA's actions are condoned, then any pre-existing secured creditor could take actions for an improper purpose or an ulterior motive in purchasing claims without fear of being found in bad faith. Actions such as TIAA's in this case frustrate the plain intent of the Code to encourage reorganizations and give debtors a fresh start.

Conflict of Interest and Unfair Discrimination.

Contrary to the rulings below, as a matter of law, TIAA acted in bad faith because it has a conflict of interest with Figter's unsecured creditors and because TIAA unfairly discriminated against the nonselling creditors. *See, e.g., In re P-R Holding Corp., supra*, 147 F.2d at 897-898 (decided under the Act, found bad faith exists when claims purchases result in discrimination in favor of the creditors selling their interests); *Applegate, supra*, 133 B.R. at 833 (decided under the Code, finding that there is bad faith where the purchase of claims results in discrimination in favor of creditors selling their interests).

Here, TIAA has been determined by the Bankruptcy Court to be fully secured and thus has no unsecured deficiency claim. Although the Ninth Circuit Opinion justified TIAA's claims purchases as being in furtherance of its purported interest as a secured creditor (App. A8), the claims TIAA purchased were unsecured claims *outside its class and in which TIAA did not previously belong*. The result is to give selling creditors 100% of their claims, whereas the Plan only provided for an 80% distribution. Thus, the nonselling creditors were unfairly discriminated against by TIAA's purchases, since they would have received only 80% and not 100% on account of their claims.

The House Report accompanying the bill enacting the Code, with regard to Section 1126(e), specifically makes reference to potential conflicts of interest by claimants purchasing claims outside their own class:

> A person might have such a conflict, for example, where he held a claim or interest in more than one class. Exclusion from one class for voting purposes would not require his exclusion from the other class as well. The result is to overrule cases such as *Aladdin Hotel Corp. v. Bloom*, 200 F.2d 627 (8th Cir. 1953), which, though not in the bankruptcy context, would appear to count votes for a reorganization plan motivated by an attempt to squeeze out a minority of a class. In that case, the conflict of interest of those voting for the plan was clear, but the court permitted the votes.

H.R. Rep. No. 595, 95th Cong., 1st Sess. 411 (1977). *See also In re Dune Deck Owners Corp.*, 175 B.R. 839, 845 n.13 (Bankr. S.D.N.Y. 1995) (noting that a court "can designate the vote of a creditor who has a conflict of interest with the class in which it votes").[2]

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[2] The Court in *Allegheny* recognized the importance of the conflict of interest issue in its decision. It stated, in this regard: "Again, we

(continued)

In the treatise J. Queenan, *et al., Chapter 11 Theory and Practice: A Guide To Reorganization*, Section 30.25 at 30:101 *et seq.* (1994) ("*Queenan*"), the authors make it clear that, even where a creditor purchases claims to advance its own interests, it may not do so where a conflict of interest exists and especially where such conflict is not adequately disclosed to the creditor class whose claims are being purchased. In this regard, among other things, *Queenan* notes that an objectionable conflict of interest can exist where a claims purchaser "seeks to frustrate a cause of action;" is motivated by interests which conflict with the debtor's plan of reorganization; fails to disclose important facts in its purchasing program due to the lack of a court-approved disclosure statement; discriminates against creditors not selling their claims; or is a plan proponent.

Thus, TIAA clearly had a conflict of interest in purchasing some, but not all, of the claims outside the class to which it did not previously belong, and thereby unfairly discriminated against such non-selling creditors. The Ninth Circuit Opinion attempted to justify such discrimination by noting that various creditors did not sell to TIAA. Neither the Ninth Circuit Opinion nor any statute or any other case, however, *requires* a secured creditor seeking to acquire a blocking position to buy 100% of the claims in a particular class for 100% of the value of each claim. Thus, the clear conflict of interest and the potential for unfair discrimination inherent in such claims purchases will continue unless the Ninth Circuit Opinion is reversed.

(fn. continued)
note that the two classes in which Japonica purchased claims have *directly opposite interests* with respect to the bank litigation. The court is hard pressed to characterize Japonica's actions as merely furthering their own economic interests." 118 B.R. at 290 (emphasis added).

Purchasing Claims Designed to Frustrate or Impede Pending Litigation Constitutes Evidence of Bad Faith.

The Ninth Circuit Opinion erred in affirming the rulings below insofar as they held that bad faith under Section 1126(e) somehow requires that a claims purchaser's *sole* intent had to be to eliminate, not merely adversely impact or frustrate in any fashion, pending litigation between it and a debtor. (App. B3, C22). These holdings are contrary to clear authority holding otherwise.

Pending litigation between the parties, in and of itself, may not warrant a finding of bad faith. However, such fact, particularly when combined with all the other indicia of bad faith in this case, constitutes strong evidence of bad faith. *See, e.g., In re Keyworth*, 47 B.R. 966, 971-972 (D.Col. 1985) (a noncreditor found to have purchased claim because it thought it could have a less litigious trustee undertake the prosecution of the personal injury case or lessen the incentive of the debtor to litigate the personal injury action by the debtor against the claims purchaser). *See also Allegheny, supra*, 118 B.R. at 290; *In re Dune Deck Owners Corp., supra*, 175 B.R. at 845 n.10 (criticizing the proposition that a creditor "can always vote against a plan without any danger of disqualification" and reasoning that buying claims in an attempt to thwart pending litigation is an ulterior motive in claims trading where its effect on the litigation is not speculative and where rejection of the plan will have an adverse impact upon the debtor's ability to continue the litigation).

Here, the Debtor is presently prosecuting the Adversary Proceeding. By precluding confirmation of the Plan, the claims purchases adversely impact the Adversary Proceeding and will frustrate, impede or deter Figter from successfully prosecuting its action against TIAA. TIAA's blocking confirmation of the Plan will have the effect of taking any

incentive and financial capability Figter has to prosecute the Adversary Proceeding. Further, TIAA's purchase of unsecured claims creates a conflict between TIAA and the unsecured creditors who will be among the beneficiaries of any judgment obtained by Figter against TIAA. Therefore, although purchasing the claims to frustrate the pending litigation, when standing alone, may not compel designation of TIAA's unsecured claims as nonvoting, it is evidence of bad faith and, when viewed with the other indicia of bad faith in this case, a finding of bad faith should have been made.

TIAA Is in Any Event Entitled to Only One Vote for Each of the Unsecured Claims Purchased.

As a historical and general rule, in a variety of pre-Code contexts, the assignee or holder of multiple claims in the same class has only one vote for purposes of voting in a bankruptcy proceeding. *See, e.g., In re Frank*, 9 F.Cas. 704, nn. 2, 3 (N.D.N.Y. 1871) (No. 5,050) (under the Bankruptcy Act of 1867, a creditor that purchased claims only had one vote in determining whether a "majority in number" of creditors had voted in favor of the election of an assignee); *In re Messengill*, 113 F. 366, 367 (E.D.N.C. 1902) (in determining whether a majority of creditors voted in favor of a "plan of composition" under the Act, the purchaser of a large number of claims was counted as one creditor); *In re Columbia Iron Works*, 142 F. 234, 242 (E.D. Mich. 1904) (under the Act, creditor only had one vote for bankruptcy trustee where creditor had been assigned multiple claims, following *Frank* and *Messengill, supra*); and *In re E.T. Kenney Co.*, 136 F. 451, 455 (D.Ind. 1905) (under the Act, committee which was assignee of 118 claims was counted as only one creditor in the election of a trustee, to prevent control of the election). *See also In re Latham Lithographic Corp.*, 107 F.2d 749, 751 (2d Cir. 1939) (under the Act, each

creditor is entitled to one vote on bankruptcy trustee, and additional creditors cannot be created by assignment). The continuing viability of *Latham*, on other points of law, was reaffirmed by the Advisory Committee to Congress when amendments were enacted to Rule 3001(e) of the Federal Rules of Bankruptcy Procedure relating to transferred claims. 11 U.S.C. app. at 247 (1988).

More recently, a Bankruptcy Court has held that, for the purposes of determining whether there are sufficient creditors to allow an involuntary Chapter 7 petition to be filed, the joint holders of the same claim must be considered to have only one claim. *In re Averil, Inc.*, 33 B.R. 562, 563 (Bankr. S.D. Fla. 1983). *See also In re Gilbert*, 115 B.R. 458, 461-462 (Bankr. S.D.N.Y. 1990) (holding that multiple claims purchased prior to the commencement of involuntary bankruptcy proceedings would be treated as one claim for purposes of determining the number of creditors necessary to file an involuntary Chapter 7 petition, the Court noting that, "[t]he courts have historically supported the concept that one creditor cannot create additional creditors by treating separate claims as separate creditors"). By analogy, for purposes of voting, a creditor who purchases multiple claims within a given class should be entitled to only one vote, in an aggregate amount, within that class. To hold otherwise would pervert the reorganization process and invite the kind of claims trading abuse engaged here by TIAA.

Legal commentators analyzing the case law and predecessor statutes from which the Code was derived have concluded that the purchaser of multiple claims has only one vote with regard to a Chapter 11 plan. Chapter XI of the Act used a "number and amount" test identical to the current Section 1126(c) test for counting votes towards plan confirmation. 52 Stat. 840, 868-869 (repealed effective 1979). The "numbers and amount" test for plan confirmation voting in Chapter XI did not address the situation where a creditor purchased multiple claims. Congress did attempt to deal

with the issue of voting multiple purchased claims in Chapter X of the Act by not requiring a majority of the number of claims for plan approval, but only requiring an affirmative vote of two-thirds in amount of claims in a given class. *Collier's* at 94-106.

Collier's goes on to note that this distinction between the voting procedures in Chapter XI and Chapter X is of crucial importance in the context of voting multiple claims in a Chapter 11 reorganization because Chapter 11 utilizes the old Chapter XI "numbers and amount" test (majority in number and two-thirds in amount). *Id.* The legislative history is devoid of any discussion as to the consequences of adopting the "numbers and amount" test as opposed to the old Chapter X two-thirds amount test. *Id.* In the absence of any legislative discussions to the contrary, *Collier's* reasons that:

> The Bankruptcy Reform Act of 1978 adopted the old Chapter XI standards for accepting a plan: two-thirds in amount and a majority in number. There is no indication in the legislative history either that Congress understood the consequences of adopting the Chapter XI test or that Congress considered the difference between counting votes in Chapter X and doing so in Chapter XI. Given the precedents under Section 12 [of the Act], however, and given that the relevant language in section 1126(c) is virtually identical to the language of Section 12, the law appears to be that the purchaser of multiple claims — even if these multiple claims are multiple debentures, notes or bonds — is to be counted as having only one vote on a plan of reorganization.

Collier's at 94-106 to 94-107.

As discussed, the Ninth Circuit Opinion to the contrary was as though the Code was a completely "clean slate" and enacted in a statutory vacuum. Not only is such an approach counter-intuitive, but it also flies in the face of a long line of

jurisprudence which cautions the Federal courts against an approach which ignores precedent and the statutory frameworks which existed prior to the enactment of the Code. In *Dewsnup v. Timm, supra*, 502 U.S. at 419-420, the Court held that, unless there is a discussion to the contrary in the legislative history, the Code is not to be construed as intending "to effect a major change in pre-Code practice."

Contrary to the finding of the Court of Appeals, the plain language of Section 1126(c) does not give a creditor a right to vote multiple claims and does not bar any inquiry into pre-Code case law. Even though Section 1126(c) refers to allowed "claims," that Section simply does not attempt to address the situation of how claims should be counted in the context of claims trading or where a given creditor holds multiple claims. Despite this, the Court of Appeals and the courts below embarked upon a "major change in pre-Code practice," by rejecting analogous bankruptcy precedent decided in a variety of analogous contexts, and in the context of the predecessor statutes to Chapter 11 of the Code, without even the slightest reference to any legislative history which might justify such a departure.

In the absence of unambiguous language addressing the issue of how many claims a multiple claims purchaser should be deemed to have for purposes of voting on a plan, the Court of Appeals and the courts below adopted broad new rules of voting, simply on the basis of the use of the word "claims" in Section 1126(c) as opposed to the words "claimants" or "creditors." In order to be consistent with *Dewsnup*, there would have to be a much clearer indication of intent on the part of Congress to abrogate the prior case law and statutory rules which governed voting in a variety of previous statutory contexts and, most importantly, in the context which is perhaps most analogous to Chapter 11, that of voting with regard to a "plan of composition" under the Act. *See, e.g., In re Messengill, supra*, 113 F. at 367. *See also Collier's* at 94-104 *et. seq.*

Not only would reversing the Court of Appeals on the "one vote rule" be consistent with pre-Code precedent, practice and predecessor statutes, but such a holding would also further the preservation of the integrity of the reorganization process. If this Court were to reverse the Court of Appeals and adopt such a rule, at the very least, secured creditors such as TIAA would be forced to purchase not just the smallest claims in the unsecured class, in an effort to control the voting of the number of claims, but also a sufficient amount to control at least one-third in the amount of the claims. In this manner, the discriminatory effect of the claims trading would be mitigated somewhat and the secured creditor would be forced to be more evenhanded in offering to purchase claims and forced to, perhaps, pay a fairer price for the claims it purchases.

Therefore, in the event that this Court does not reverse the ruling below that the claims purchased by TIAA were not purchased in bad faith, this Court should nonetheless reverse the holding that TIAA is entitled to one vote for each claim purchased and decide that TIAA is only entitled to one vote by virtue of the multiple unsecured claims which it holds.

The Court of Appeals Applied the Wrong Standard of Review.

All of the above issues are issues of law or of mixed law and fact to be reviewed *de novo* by the Court of Appeals, in accordance with the applicable case law in the Ninth Circuit. *In re Kissinger (Mataya v. Kissinger)*, 72 F.3d 107, 108 (9th Cir. 1995); *In re Weisman (Robertson v. Peters)*, 5 F.3d 417, 419 (9th Cir. 1993); *National Ass'n of Radiation Survivors v. Derwinski*, 994 F.2d 583, 587 (9th Cir. 1992) (mixed issue of law and fact to be reviewed *de novo*); *Boone v. United States*, 944 F.2d 1489, 1492 (9th Cir. 1991) (same). *See also, e.g., Bogardus v. Commissioner*, 302 U.S. 34, 39 (1937) (indicating *de novo* review with respect to mixed questions

of fact and law). As a threshold matter, the Court of Appeals stated that it reviewed the District Court's good faith determination on a "clearly erroneous" standard. (App. A4). All issues presented below were either questions of law or mixed questions of fact and law, requiring a *de novo* review. In particular, the bad faith issue is a "mixed" issue of law and fact which even the Ninth Circuit Opinion stated is to be reviewed *de novo*. App. A4; *National Ass'n of Radiation Survivors v. Derwinski, supra*, 994 F.2d at 587; *Boone v. United States, supra*, 944 F.2d at 1492. A mixed question of law and fact is presented where "the historical facts are established, the rule of law is undisputed, and the issue is whether the facts satisfy the legal rule." *Pullman-Standard v. Swint*, 456 U.S. 273, 289 n.19 (1982). At the very least, therefore, if certiorari is granted but reversal of the Ninth Circuit Opinion is not, the case should be remanded to the Court of Appeals to review the entire District Court Order *de novo*.

CONCLUSION

This Court should grant certiorari to determine as a matter of law whether the claims purchases at issue were in bad faith within the meaning of Section 1126(e) of the Code or, alternatively, to determine that a purchaser of claims under the Code should be entitled to only one vote as to the claims it purchased.

DATED: September 19, 1997.

Respectfully submitted,

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APPENDIX A

FOR PUBLICATION

UNITED STATES COURT OF APPEALS
FOR THE NINTH CIRCUIT

In re: FIGTER LIMITED,
Debtor.

FIGTER LIMITED,
Appellant,
v.
TEACHERS INSURANCE AND ANNUITY ASSOCIATION OF AMERICA,
Appellee.

No. 96-55356
D.C. No. CV-95-04462-SVW
OPINION

Appeal from the United States District Court
for the Central District of California
Stephen V. Wilson, District Judge, Presiding

Argued and Submitted
June 6, 1997—Pasadena, California

Filed June 24, 1997

Before: Procter Hug, Jr., Chief Judge, and
Ferdinand F. Fernandez and Pamela Ann Rymer,
Circuit Judges.

Opinion by Judge Fernandez

OPINION

FERNANDEZ, Circuit Judge:

Figter Limited, a Chapter 11 debtor and owner of Skyline Terrace, an apartment complex, appeals from the district court's affirmance of the bankruptcy court's decision that Teachers Insurance and Annuity Association of America (Teachers), the holder of a $15,600,000 promissory note secured by a first deed of trust on Skyline Terrace, bought twenty-one unsecured claims in good faith and that it could vote each one separately. We affirm.

BACKGROUND

Figter filed a voluntary petition under Chapter 11 of the Bankruptcy Code. It owns Skyline Terrace, a 198-unit residential apartment complex located in Los Angeles. Teachers is a creditor. It holds a $15,600,000 promissory note executed by Figter. The note is secured by a first deed of trust on Skyline Terrace and by $1,400,000 of cash on hand. In fact, Teachers is Figter's only secured creditor and is the only member of Class 2 in a reorganization plan proposed by Figter. The plan contemplates full payment of Teachers' secured claim, but at a disputed rate of interest. Thus, under Figter's plan, Teachers' claim is not impaired. The plan calls for the impairment of Class 3 unsecured claims by payment at only 80% of their face value.

Teachers has opposed Figter's reorganization plan from its inception because, among other things, that plan contemplates the conversion of Skyline Terrace Apartments into condominiums, with payment to and partial releases by Teachers as the units sell. That could easily result in a property that was part condominium and part rentals, if the plan ultimately fails in operation.

Teachers proposed a plan of its own, which provided for the transfer of Skyline Terrace and the cash collateral to

Teachers in satisfaction of its secured claim, as well as a payment of Class 3 unsecured claims at 90%. Teachers' plan was premised on the assumption that its claim was partly unsecured. However, on May 31, 1994, before the purchases of other claims took place, the bankruptcy court determined that Skyline Terrace had a value of $19,300,000. Thus, Teachers' claim in the amount of $17,960,000 was fully secured. It did not thereafter pursue its plan. From October 27, 1994 until October 31, 1994, Teachers purchased twenty-one of the thirty-four unsecured claims in Class 3 at one hundred cents on the dollar, for a total purchase price of $14,588.62. Teachers had made the same offer to all of the Class 3 claim holders, but not all accepted it. The offer remained open. Teachers then filed notices of transfer of claims with the court, as is required under Bankruptcy Rule 3001(e)(2). Those notices were served on all affected parties, including Figter. No objections were filed by the unsecured creditors. The district court upheld the bankruptcy court's determination regarding Teachers' purchase of the unsecured claims. As a result, Figter's plan is unconfirmable because it is unable to meet the requirements of 11 U.S.C. § 1129(a)(10); there will not be an impaired, consenting class of claims. That will preclude a "cram down" of Teachers' secured claim under 11 U.S.C. § 1129(b). Figter has appealed in an attempt to avoid that result.

STANDARD OF REVIEW

We do not give deference to the district court's decision or determinations. *See Friedkin v. Sternberg (In re Sternberg)*, 85 F.3d 1400, 1404 (9th Cir. 1996); *Robertson v. Peters (In re Weisman)*, 5 F.3d 417, 419 (9th Cir. 1993); *Wein Air Alaska, Inc. v. Bachner*, 865 F.2d 1106, 1108 (9th Cir. 1989). However, we review the bankruptcy court's conclusions of law de novo and uphold its findings of fact unless they are clearly erroneous. *See Feder v. Lazar (In re Lazar)*, 83 F.3d 306, 308 (9th Cir. 1996); *Weisman*, 5 F.3d at 419. Here we are asked to review the bankruptcy court's determination that

Teachers acted in good faith when it purchased the claims of certain creditors and that it can vote each one separately.

[1] To the extent that our review requires us to define the general parameters of a good faith determination, we are reviewing a question of law. To the extent that we must review a pure historical fact determination, we are reviewing a question of fact. *See Boone v. United States*, 944 F.2d 1489, 1492 (9th Cir. 1991). But, a determination of good faith can partake of both, and we often review mixed questions of law and fact de novo. *See id.* Nevertheless, a decision that someone did or did not act in good faith is one where the determination is "an essentially factual inquiry" and is driven by the "data of practical human experience." *United States v. McConney*, 728 F.2d 1195, 1203-04 (9th Cir. 1984) (en banc) (citations omitted). For that reason, we have, in various contexts, declared that we will review good faith determinations for clear error. *See, e.g., L. K. Comstock & Co., Inc. v. United Eng'rs & Constructors Inc.*, 880 F.2d 219, 232 (9th Cir. 1989) (decision regarding "good faith" for covenant of good faith and fair dealing purposes is reviewed for clear error); *Mortgage Mart, Inc. v. Rechnitzer (In re Chisum)*, 847 F.2d 597, 600 (9th Cir. 1988) (for sanctions purposes "good faith" is a key factual determination reviewed for clear error); *cf. SKS Die Casting and Machining, Inc. v. NLRB*, 941 F.2d 984, 991 (9th Cir. 1991) (NLRB decision regarding "good faith" bargaining is a mixed question of law and fact which we review for substantial evidence). Therefore, we will review the bankruptcy court's ultimate good faith determination for clear error.

DISCUSSION

Figter asserts that Teachers should be precluded from voting its purchased Class 3 claims because it did not buy them in good faith. Figter also asserts that even if the claims were purchased in good faith, Teachers cannot vote them separately, but is limited to one total vote as a Class 3 creditor. If

Figter were correct in either of its assertions, it could obtain Class 3 approval of its plan and enhance its chances of cramming down Teachers' Class 2 claims. But Figter is not correct.

A. *Good Faith.*

[2] The Bankruptcy Code provides that "[o]n request of a party in interest, and after notice and a hearing, the court may designate any entity whose acceptance or rejection of [a] plan was not in good faith, or was not solicited or procured in good faith or in accordance with the provisions of this title." 11 U.S.C. § 1126(e). In this context, designate means disqualify from voting. The Bankruptcy Code does not further define the rather murky term "good faith." That job has been left to the courts.

The Supreme Court brought some clarity to this area when it decided *Young v. Higbee Co.*, 324 U.S. 204, 65 S. Ct. 594, 89 L. Ed. 890 (1945). In *Young*, the Court was discussing the predecessor to § 1126(e) when it declared that if certain persons "had declined to accept [the] plan in bad faith, the court, under section 203 could have denied them the right to vote on the plan at all." *Id.* at 210-11, 65 S. Ct. at 598 (footnote omitted). It went on to explain that the provision was intended to apply to those "whose selfish purpose was to obstruct a fair and feasible reorganization in the hope that someone would pay them more than the ratable equivalent of their proportionate part of the bankrupt assets." *Id.* at 211, 65 S. Ct. at 598. In other words, the section was intended to apply to those who were not attempting to protect their own proper interests, but who were, instead, attempting to obtain some benefit to which they were not entitled. *See also Insinger Machine Co. v. Federal Support Co. (In re Federal Support Co.)*, 859 F.2d 17, 19 (4th Cir. 1988). While helpful, those reflections by the Court do not fully answer the question before us. Other courts have further illuminated the area.

[3] If a person seeks to secure some untoward advantage over other creditors for some ulterior motive, that will indicate bad faith. *See In re Marin Town Ctr.*, 142 B.R. 374, 378-79 (N.D. Cal. 1992). But that does not mean that creditors are expected to approach reorganization plan votes with a high degree of altruism and with the desire to help the debtor and their fellow creditors. Far from it.

> If a selfish motive were sufficient to condemn reorganization policies of interested parties, very few, if any, would pass muster. On the other hand, pure malice, "strikes" and blackmail, and the purpose to destroy an enterprise in order to advance the interests of a competing business, all plainly constituting bad faith, are motives which may be accurately described as ulterior.

In re Pine Hill Collieries Co., 46 F. Supp. 669, 671 (E.D. Pa. 1942). That is to say, we do not condemn mere enlightened self interest, even if it appears selfish to those who do not benefit from it. *See id.*

[4] Thus, if Teachers acted out of enlightened self interest, it is not to be condemned simply because it frustrated Figter's desires. That is true, even if Teachers purchased Class 3 claims for the very purpose of blocking confirmation of Figter's proposed plan. *See 255 Park Plaza Assocs. Ltd. Partnership v. Connecticut General Life Ins. Co. (In re 255 Park Plaza Assocs. Ltd. Partnership)*, 100 F.3d 1214, 1218-19 (6th Cir. 1996). That self interest can extend even further without being an ulterior motive. It has been held that a creditor commits no wrong when he votes against a plan of a debtor who has a lawsuit pending against the creditor, for that will not, by itself, show bad faith. *See Federal Support Co.*, 859 F.2d at 20; *see also In re A.D.W., Inc.*, 90 B.R. 645, 651 (Bankr. D. N.J. 1988); *In re Landau Boat Co.*, 8 B.R. 432, 436 (Bankr. W.D. Mo. 1981). It has also been held that no bad faith is shown when a creditor chooses to benefit his interest as a

creditor as opposed to some unrelated interest. *See In re Landing Assocs., Ltd.*, 157 B.R. 791, 803 (Bankr. W.D. Tex. 1993); *In re Peter Thompson Assocs., Inc.*, 155 B.R. 20, 22 (Bankr. D. N.H. 1993). And the mere fact that a creditor has purchased additional claims for the purpose of protecting his own existing claim does not demonstrate bad faith or an ulterior motive. "As long as a creditor acts to preserve what he reasonably perceives as his fair share of the debtor's estate, bad faith will not be attributed to his purchase of claims to control a class vote." *In re Gilbert*, 104 B.R. 206, 217 (Bankr. W.D. Mo. 1989).

[5] Courts, on the other hand, have been sensitive to situations where a company, which was not a preexisting creditor, has purchased a claim for the purpose of blocking an action against it. They have seen that as an indication of bad faith. *See In re Keyworth*, 47 B.R. 966, 971-72 (Bankr. D. Colo. 1985). The same has been true where creditors were associated with a competing business and desired to destroy the debtor's business in order to further their own. *See In re MacLeod Co., Inc.*, 63 B.R. 654, 655 (Bankr. S.D. Ohio 1986); *see also In re Allegheny Int'l, Inc.*, 118 B.R. 282, 289 (Bankr. W.D. Pa. 1990). And when the debtor had claims against itself purchased by an insider or affiliate for the purpose of blocking a plan, or fostering one, that was seen as a badge of bad faith. *See In re Holly Knoll Partnership*, 167 B.R. 381, 389 (Bankr. E.D. Pa. 1994) (fostering); *In re Applegate Property, Ltd.*, 133 B.R. 827, 834-35 (Bankr. W.D. Tex. 1991) (blocking). Figter would have us add that in a single asset bankruptcy, claim purchasing activities, like those of Teachers, are in bad faith. It cites no authority for that, and we see no basis for establishing *that* as a per se rule.

In short, the concept of good faith is a fluid one, and no single factor can be said to inexorably demand an ultimate result, nor must a single set of factors be considered. It is always necessary to keep in mind the difference between a creditor's self interest as a creditor and a motive which is ulterior to the

purpose of protecting a creditor's interest. Prior cases can offer guidance, but, when all is said and done, the bankruptcy court must simply approach each good faith determination with a perspicacity derived from the data of its informed practical experience in dealing with bankrupts and their creditors.

[6] Here, the bankruptcy court did exactly that. It decided that Teachers was not, for practical purposes, the proponent of an alternate plan when it sought to purchase the Class 3 claims. Nor, it found, did Teachers seek to purchase a small number of claims for the purpose of blocking Figter's plan, while injuring other creditors, even if it could do that in some circumstances. Rather, Teachers offered to purchase all Class 3 claims, and only some of those claimants' refusals to sell precluded it from doing so. Moreover, Teachers was a lender, not a competing apartment owner. It acted to protect its interests as Figter's major creditor. It reasonably feared that it could be left with a very complex lien situation, if Figter went forward with its plan. Instead of holding a lien covering the whole of the property, it could have wound up with separate fractured liens on various parts of the property, while other parts were owned by others. That could create a very undesirable mix of owners and renters and of debtors and nondebtors. Added to that was the actual use of cash, which was collateral for the debt owed to Teachers. It cannot be said that Teachers' concerns were irrational.

Based on all that was before it, the bankruptcy court decided that in this case Teachers was a creditor which acted in a good faith attempt to protect its interests and not with some ulterior motive. We cannot say that it erred in making that ultimate determination.

B. *Voting.*

[7] Figter's fallback position is that even if Teachers did act in good faith, it must be limited to one vote for its twenty-one

claims. That assertion is answered by the language of the Bankruptcy Code, which provides that:

> A class of claims has accepted a plan if such plan has been accepted by creditors . . . that hold at least two-thirds in amount and *more than one-half in number of the allowed claims* of such class held by creditors . . . that have accepted or rejected such plan.

11 U.S.C. § 1126(c) (emphasis added). That language was interpreted in *Gilbert*, 104 B.R. at 211, where the court reasoned:

> The formula contained in Section 1126(c) speaks in terms of the *number of claims*, not the number of creditors, that actually vote for or against the plan. . . . Each claim arose out of a separate transaction, evidencing separate obligations for which separate proofs of claim were filed. Votes of acceptance . . . are to be computed only on the basis of filed and allowed proofs of claim. . . . [The creditor] is entitled to one vote for each of his unsecured Class X claims.

That same view was iterated in *Concord Square Apartments of Wood Cty, Ltd. v. Ottawa Properties, Inc. (In re Concord Square Apartments of Wood Cty., Ltd.)*, 174 B.R. 71, 74 (Bankr. S.D. Ohio 1994), where the court held that a creditor with "multiple claims, has a voting right for each claim it holds." We agree. It would not make much sense to require a vote by creditors who held "more than one-half in number of the allowed claims" while at the same time limiting a creditor who held two or more of those claims to only one vote. If allowed claims are to be counted, they must be counted regardless of whose hands they happen to be in.

Figter seeks some succor from the Supreme Court's indication in *Dewsnup v. Timm*, 502 U.S. 410, 419-20, 112 S. Ct. 773, 779, 116 L. Ed. 2d 903 (1992), that ambiguous language

in the Code should not be taken to effect a sea change in pre-Code practice. However, that does not help Figter's cause. In the first place, as we have indicated, the present language is not ambiguous. In the second place, the old law to which *Figter* refers relied upon a code section which required voting approval by a "majority in number of all creditors whose claims have been allowed." Bankruptcy Act of 1898, ch. 541, § 12, 30 Stat. 544, 549-50 (*repealed* 1938); *see In re Messengill*, 113 F. 366 (E.D.N.C. 1902). It is pellucid that "a majority in number of all creditors" is not at all like "more than one-half in number" of all claims. The former focuses on claimants; the latter on claims.

Nor is our conclusion affected by cases where other sections of the bankruptcy code, or other acts by creditors, were involved. For example, the predecessor to 11 U.S.C. § 702 indicated that a creditor could vote for the trustee. In *In re Latham Lithographic Corp.*, 107 F.2d 749 (2d Cir. 1939), there was an attempt to split a single claim into multiple claims for the purpose of creating multiple creditors who could vote in a trustee election. It is not surprising that the court did not permit that. *See id.* at 751. And in *In re Gilbert*, 115 B.R. 458, 461 (Bankr. S.D.N.Y. 1990), the court held that an involuntary petition in bankruptcy must be filed by three creditors, and a single creditor with three separate claims is still one creditor. *See also In re Averil*, 33 B.R. 562, 563 (Bankr. S.D. Fla. 1983). In fact, the involuntary petition section actually requires that there be three or more *entities*. *See* 11 U.S.C. § 303(b). Certainly, a creditor with three claims is still a single entity.

[8] Of course, that is not to say that a creditor can get away with splitting one claim into many, but that is not what happened here. Teachers purchased a number of separately incurred and separately approved claims (each of which carried one vote) from different creditors. There simply is no reason to hold that those separate votes suddenly became one

vote, a result which would be exactly the opposite of claim splitting.

Therefore, the bankruptcy court did not err.

CONCLUSION

Figter hoped to obtain approval of a reorganization plan, which would require Teachers to thole what it saw as a diminution of its creditor's rights. Those hopes were dashed when Teachers bought up most of the Class 3 claims in an effort to protect its own Class 2 claim. Because the bankruptcy court determined that Teachers acted to protect its valid creditor's interest, rather than for ulterior motives, it held that Teachers had acted in good faith. That precluded designation of Teachers' purchased claims. The bankruptcy court also determined that Teachers could vote each of its twenty-one claims separately; it was not limited to a single vote. The district court affirmed those decisions. Because the bankruptcy court did not err in either its factual or its legal determinations, we agree with the district court and affirm the decision.

AFFIRMED.

APPENDIX B

UNITED STATES DISTRICT COURT
CENTRAL DISTRICT OF CALIFORNIA

FILED
Clerk, U.S. District Court
JAN 24 1996
Central District of California
By Deputy

In re
FIGTER LIMITED,
Debtor and Debtor-in Possession

FIGTER LIMITED,
Appellant,
v.
TEACHERS INSURANCE AND ANNUITY ASSOCIATION OF AMERICA,
Appellee.

DISTRICT COURT CASE NO. CV 95-4462-SVW

BANKRUPTCY COURT CASE NO. SV 93-29168-AG
(Chapter 11)

ORDER AFFIRMING DECISION
OF BANKRUPTCY COURT

TO ALL PARTIES AND THEIR ATTORNEYS OF RECORD:

I. Jurisdiction

28 U.S.C. §§ 158 and 1334 confer upon this Court the jurisdiction to review this Appeal.

II. Standard of Review

The Court regards the Bankruptcy Court's determination of good faith as a finding of both fact and law. Accordingly, with respect to the 11 U.S.C. § 1126(e) issue, findings of fact are reviewed under the clearly erroneous standard, and conclusions of law are reviewed *de novo*. *Wein Air Alaska, Inc. v. Bachner*, 865 F.2d 1106, 1108 (9th Cir. 1989). The second issue requires statutory interpretation of 11 U.S.C. § 1126(c). This issue of law is, therefore, reviewed *de novo*.

III. Affirmation of Decision with Clarification

The Court affirms the Memorandum of Decision and further clarifies the Bankruptcy Court's finding of good faith, under § 1126(e).

A. Plan Proponent

The Bankruptcy Court found that Teachers Insurance and Annuity Association of America ("Teachers") was not a Plan Proponent when it purchased the twenty-one unsecured claims. This finding is clearly supported by the record.

As the Bankruptcy Court properly recognized, Teachers' Plan, filed on February 4, 1994, was premised

on the assumption that Teachers' claim was undersecured. When, on August 24, 1994, the Bankruptcy Court determined that Teachers was, in fact, oversecured, and not undersecured, Teachers Plan was essentially moot. In fact, at the close of the valuation hearing, Teachers informed the court that in light of the Bankruptcy Court's determination, "it's likely that Teachers will not be going forward with its own plan. . ."

The record further indicates that Teachers made no attempt to amend its Plan subsequent to the August 24, 1994 valuation hearing. Together, this information supports the Bankruptcy Court's finding that Teachers was not a Plan Proponent when it purchased the unsecured claims.

B. Pending Litigation

Figter Limited ("Debtor") contended that Teachers had purchased the unsecured claims in order to frustrate the pending state and federal lawsuits between Teachers and Debtor. The Bankruptcy Court dismissed this argument on the grounds that neither suit would be *eliminated* as a result of Teachers' purchase. The Bankruptcy Court, however, did not address Debtor's argument that Teachers' purchase was intended to frustrate — not eliminate — the pending litigation.

The Court has examined this argument and has determined that it is without merit. First, a court will not find bad faith when the alleged intent to frustrate litigation is merely speculative or remote. *In re Federal Support Co.*, 859 F.2d 17, 20 (4th Cir. 1988) (pending litigation alone cannot constitute bad faith; bad faith does not exist if the alleged intent to frustrate pending litigation is speculative or remote). In the instant case, there is nothing to support the Debtor's contention that it was

Teachers' primary intention to frustrate the pending litigation. Secondly, at least one court has found that even if a creditor intended to frustrate pending litigation, no bad faith exists. *In re Lloyd McKee Motors, Inc.*, 157 Bankr. 487, 489 (Bankr. D.N.M. 1993) (the court refused to disqualify creditor's votes against a plan, even if the creditor's ulterior motive was to frustrate pending litigation). Finally, no bad faith exists where a creditor purchases claims in its own self-interest, and as an unintended side-effect of that purchase, pending litigation is actually frustrated. *In re Federal Support Co.*, 859 F.2d 17, 20 (4th Cir. 1988) ("One's self-interest . . . does not provide an ulterior motive").

IT IS ORDERED that the Bankruptcy Court's Memorandum of Decision is affirmed.

IT IS FURTHER ORDERED that the Clerk shall serve copies of this Order herein, by United States mail, on counsel for both Appellant and Appellee.

IT IS SO ORDERED.

DATED: 1/24/96

/s/ STEPHEN V. WILSON
STEPHEN V. WILSON
United States District Judge

APPENDIX C

UNITED STATES BANKRUPTCY COURT
CENTRAL DISTRICT OF CALIFORNIA

FILED
MAY 3 1995
Clerk, U.S. Bankruptcy Court
Central District of California
By Deputy Clerk

In re
FIGTER LIMITED,
Debtor and
Debtor-in-Possession.

CASE NO. LA 93-29168-AG
Chapter 11

ORDER

In accordance with this court's Memorandum of Decision filed concurrently with this order, IT IS ORDERED AND ADJUDGED that;

(1) The motion of Teachers Insurance and Annuity Association of America ("Teachers") requesting an order declaring that the purchase of unsecured claims by secured creditor Teachers was in good faith under 11 U.S.C. § 1126(e), is granted;

(2) The cross motion of Debtor, Figter Limited, seeking an order pursuant to 11 U.S.C. §§ 105 and 1126(e) designating all unsecured or other claims purchased, or to be purchase in the future, by Teachers, as being non-voting for purposes of the Debtor's proposed plan of reorganization and enjoining Teachers from purchasing any other claims in this proceeding, without an order, is denied; and

(3) Debtor's alternative request in its cross motion for an order pursuant to 11 U.S.C. §§ 105 and 1126(e) designating that all such claims held or to be held by Teachers in the future be deemed to be a single, aggregate claim for purposes of voting on the Debtor's proposed plan of reorganization, is also denied.

DATED: May 3, 1995.

/s/ ARTHUR M. GREENWALD
ARTHUR M. GREENWALD
United States Bankruptcy Judge

UNITED STATES BANKRUPTCY COURT
CENTRAL DISTRICT OF CALIFORNIA

FILED
MAY 3 1995
Clerk, U.S. Bankruptcy Court
Central District of California
By Deputy Clerk

In re
FIGTER LIMITED,
Debtor and
Debtor-in-Possession.

CASE NO. LA 93-29168-AG
Chapter 11

MEMORANDUM OF DECISION

NATURE OF PROCEEDINGS

On May 27, 1993, the Debtor, Figter Limited, filed a voluntary petition under Chapter 11 of the Bankruptcy Code.

On December 22, 1994, a continued hearing was held on the Debtor's Second Amended Disclosure Statement. At the hearing, the Debtor advised the court that it intended to challenge whether Teachers Insurance and Annuity Association of America's (Teachers) purchases of unsecured claims were made in good faith. The court directed that the claims purchase issue be resolved prior to proceeding with the Disclosure Statement and Plan confirmation process. Accordingly, the court continued the Disclosure Statement hearing to May 25, 1995.

On February 7, 1995, Teachers filed its motion for order declaring that the purchase of unsecured claims by Teacher was in good faith under 11 U.S.C. § 1126(e). On February 16, 1995, the Debtor filed its cross-motion pursuant to 11 U.S.C. § 1126(e)[1] to disqualify the unsecured claims purchased by Teachers.

Teacher's motion and the Debtor's cross-motion were heard initially on March 9, 1995, with a final evidentiary hearing being held on March 31, 1995. The motions then were submitted.

Prior to the final evidentiary hearing, Teachers and the Debtor filed a Joint Stipulation, which included general stipulations,[2] stipulated facts, contentions of the parties and requests for judicial notice. Testimony in the

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[1] Teachers' Motion and Debtor's Cross-Motion are premature, as to date no votes have been cast. Nevertheless, the disposition of these motions is appropriate at this time since Teachers has asserted that it will vote against the Debtor's Plan. *See* 11 U.S.C. § 1126(e); *In re Pleasant Hill Partners, L.P.*, 163 B.R. 388, 389 (Bankr. N.D. Ga. 1994).

[2] The general stipulations accepted by the court on March 9, 1995 and reiterated in the Joint Stipulation are as follows:

> 1. The parties hereby stipulate to the general admissibility of all Declarations filed with the Papers, which Declarations shall serve as the direct testimony of the declarants, and the parties hereby waive any right they may have to cross-examine said declarants;
>
> 2. Teachers stipulates that Mr. Cox and Mr. Prager apparently misunderstood the nature and content of the contacts they had with representatives of Teachers, although Teachers and its representatives deny any attempt to mislead Mr. Cox and/or Mr. Prager, and Mr. Gutcho reaffirms his Declarations submitted to this Court; and
>
> 3. [T]he parties will leave it up to the Court to determine the credibility of the declarants based on all the evidence and the arguments of counsel.

form of filed declarations was received by the court in accordance with the Joint Stipulation No other testimony was offered by the parties.

The parties have agreed that if Teachers is allowed to vote each of the unsecured claims it purchased, the Debtor's Plan, as currently proposed, will be unconfirmable on its face, as the Debtor will be unable to meet the requirements of 11 U.S.C. § 1129(a)(10),[3] i.e., the existence of an impaired consenting class of claims, which also would preclude a cramdown of Teachers' secured claim under § 1129(b). *See In re 266 Washington Associates*, 141 B.R. 275, 282 (Bankr. E.D. N.Y. 1992).

The court, having considered the record before it, including the declarations and documents received in evidence, the memoranda, briefs and Joint Stipulation filed by the parties, as well as the arguments of counsel, files this Memorandum of Decision, which shall constitute this court's findings of Fact and Conclusions of Law.

STATEMENT OF FACTS

The Debtor owns a 198-unit multi-family residential apartment complex (Skyline Terrace) located in downtown Los Angeles. Teachers is a pre-existing creditor by virtue of a $15.6 million promissory note executed by the Debtor in favor of Teachers on April 20, 1989. This note is secured by a first trust deed lien on Skyline Terrace. The Debtor also holds approximately $1.4 million in cash.

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[3] § 1129(a)(10) provides:

> If a class of claims is impaired under the plan, at least one class of claims that is impaired under the plan has accepted the plan, determined without including any acceptance of the plan by any insider.

Teachers is the Debtor's only secured creditor. Under the Debtor's Plan, Teachers is also the only member of Class 2. The Plan contemplates the full payment of Teachers' secured claim over time at a market rate of interest.

The Debtor's Plan provides for the impairment of the Class 3 general unsecured claims by paying eighty percent of the allowed amount of these claims. Also, the Debtor's Plan provides for the conversion of the Skyline Terrace apartments into condominiums, and a condominium sales program of approximately three years, with Teachers to release portions of its lien as individual condominiums are sold.

Teachers has opposed the Debtor's Plan from its inception contending, among other objections, that the Plan does not meet the cramdown provisions of 11 U.S.C. § 1129(b). Teachers has made numerous objections to the Disclosure Statement and has requested relief from stay, the latter being withdrawn without prejudice.

The Debtor commenced a lender liability action against Teachers, filing an adversary proceeding on or about December 14, 1993, having previously been involved in a similar action against Teachers in the State court. The adversary proceeding was stayed by order of this bankruptcy court until June 27, 1995. The State court action has been stayed as a result of the filing of this Chapter 11 bankruptcy case.

The Debtor initially filed its Plan and Disclosure Statement on or about December 23, 1993. The Debtor's Plan was premised on the Debtor's contention that Teachers' claim was oversecured. Subsequent to this court's order denying the Debtor's request to extend the exclusivity period for filing and accepting a plan of reorganization, Teacher filed its own Plan and Disclosure Statement on February 4, 1994.

Teachers' Plan provided for the transfer of Skyline Terrace and all cash collateral to Teachers in satisfaction of its secured claim, along with the payment of ninety percent of the allowed amounts of all Class 3 claimants. Teachers' Plan was premised on Teachers' contention that its claim was undersecured.

Commencing on or about May 25, 1994 and continuing through August 24, 1994, this court conducted evidentiary hearings pursuant to 11 U.S.C. § 506(a).[4] Based ultimately upon a stipulation submitted by the parties, this court determined that as of May 31, 1994, the value of Skyline Terrace was approximately $19.3 million and that as of May 31, 1994, Teachers had a

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[4] Section 506(a) provides:

> Determination of secured status.
>
> (a) An allowed claim of a creditor secured by a lien on property in which the estate has an interest, or that is subject to setoff under section 553 of this title, is a secured claim to the extent of the value of such creditor's interest in the estate's interest in such property, or to the extent of the amount subject to setoff, as the case may be, and is an unsecured claim to the extent that the value of such creditor's interest or the amount so subject to setoff is less than the amount of such allowed claim. Such value shall be determined in light of the purpose of the valuation and of the proposed disposition or use of such property, and in conjunction with any hearing on such disposition or use or on a plan affecting such creditor's interest.

Bankruptcy Rule 3012 provides:

> Valuation of Security.
>
> The court may determine the value of a claim secured by a lien on property in which the estate has an interest on motion of any party in interest and after a hearing on notice to the holder of the secured claim and any other entity as the court may direct.

fully secured claim in the amount of approximately $17.96 million.

At the August 24, 1994 hearing, the court established October 24, 1994 as the last day for either party to file amended Disclosure Statements. The October 24, 1994 date was extended to November 11, 1994 pursuant to a stipulation executed by the parties and approved by the court. Teachers did not file any amended Plan or Disclosure Statement by November 11, 1994, nor has Teachers offered to file any amended Plan or Disclosure Statement since that date.

In order to reflect the results of the valuation hearing, the Debtor filed its First Amended Disclosure Statement on November 14, 1994. At the December 8, 1994 hearing, Teachers advised the court that it was withdrawing its Plan and Disclosure Statement. On December 16, 1994, Teachers filed and served its notice of withdrawal of its Plan and Disclosure Statement.

During the period October 27, 1994 through October 31, 1994, Teachers purchased twenty-one of the thirty-six unsecured claims classified in Class 3 at one-hundred cents on the dollar for a total of $14,588.62. Teachers did not advise the Debtor, nor the court prior to the purchases in question, that it had acquired the twenty-one claims.

On or about November 23, 1994, Teachers filed with the Clerk of the Court Notices of Transfer of Claim as required by Bankruptcy Rule 3001(e)(2). On or about December 14, 1994, the Clerk of the Court served its Notice of Transfer of Claims on Teachers, the transferors, and Debtor. No objection was filed by any transferor within the twenty-day period provided for in Rule 3001(e)(2).

Debtor was not aware of the claims purchases until a few days prior to the December 22, 1994 hearing on

Debtor's Second Amended Disclosure, when it received the Notices of Transfer of Claims served by the Clerk of the Court.

ISSUES PRESENTED

Whether Teachers acted in good faith in purchasing the twenty-one unsecured claims.

Whether Teachers is entitled to one Class 3 vote for each of the twenty-one unsecured claims purchased.

DECISION

Teachers' purchase of the twenty-one unsecured claims in Class 3 of the Debtor's Plan was made in good faith. Teachers is entitled to one vote for each of the twenty-one claims purchased.

DISCUSSION

Teachers' Purchase Of The Twenty-One Unsecured Claims Was Made In Good Faith

The Legal Standard Applicable To § 1126(e)

Section 1126(e) of the Bankruptcy Code provides, in pertinent part, as follows:

> On request of a party in interest, and after notice and a hearing, the court may designate [i.e. disqualify] any entity whose acceptance or rejection of such plan was not in good faith, or was not solicited or procured in good faith or in accordance with the provisions of this title. (insert added).

Section 1126(e) was derived from § 203 of the Bankruptcy Act of 1898 and Chapter X Rule 10-305(d) of the Rules of Bankruptcy Procedure. As stated by the court in the case of *In re Pleasant Hill Partners, L.P.*, 163 B.R. 388, 393 (Bankr. N.D. Ga. 1994):

> The legislative history of § 1126(e) shows that it was derived from § 203[9] of the Bankruptcy Act and Rule 10-305(d).[10] The promulgation of § 203 and Rule 10-305(d) was designed to discourage:
>
> > a fellow [who] goes out and buys securities at a default price and then sits back in a nuisance or strategic position and seeks to capitalize on that. It also covers the situation where he does not buy at a default price, but nevertheless is working a holdup scheme on those who are trying to get these securities in during reorganization.
>
> H.R. 6439, 75th Cong., 1st Sess. 184-4 (1937). Congress did not intend, however, to prohibit creditors form [sic] voting selfishly. "Self interest is not the same as ulterior motive or bad faith." *Kremer v. Clark (In re Frank Fehr Brewing Co.)*, 268 F.2d 170, 180 (6th Cir. 1959). *See also, In re Pine Hill Collieries Co.*, 46 F.Supp. 669 (E.D.Penn. 1942).
>
> [9] Section 203 provided:
>
> > If the acceptance or failure to accept a plan by the holder of any claim or stock is not in good faith, in the light of or irrespective of the time of acquisition thereof, the judge may, after hearing upon notice, direct that

> such claim or stock be disqualified for the purpose of determining the requisite majority for the acceptance of the plan.

[10] Rule 10-305(d) provided:

> For the purpose of determining the requisite number of acceptances, the court after hearing on notice to the creditor or stockholder may disqualify any acceptance or rejection of a plan or modification of a plan if such acceptance or rejection was not in good faith in the light of or irrespective of the time of the acquisition of the claim or stock by such creditor or stockholder.

The term good faith was left undefined in either the Bankruptcy Act of 1898 or the Rules of Bankruptcy Procedure. It was intended that the meaning of the term good faith be developed and construed on a case by case basis. 5 *Collier on Bankruptcy* ¶ 1126.05, at 1126-19 (15th ed. 1994). Good faith remains undefined under the current Bankruptcy Code. Therefore, the analysis in the instant case must focus on the development and construction of the term good faith under the case law interpreting § 203, Chapter X Rule 10-305(d) and the current Bankruptcy Code.

The United States Supreme Court considered the standard for good faith under §203 of the Bankruptcy Act of 1898 in the case of *Young v. Higbee Co.*, 324 U.S. 204, 211, 65 S.Ct. 594, 597-98, 89 L.Ed. 890, 896-97 (1945), stating in pertinent part:

> The history of this provision [§ 203] makes clear that it was intended to apply to those stockholders whose selfish purpose was to

> obstruct a fair and feasible reorganization in the hope that someone would pay them more than the ratable equivalent of their proportionate part of the bankrupt assets. (insert added)

Elaborating upon this statement, the United States Supreme Court stated as follows regarding good faith:

> To this end they adopted the "good faith" provisions of §203. Its purpose was to prevent creditors from participating who "by the use of obstructive tactics and hold-up techniques exact for themselves undue advantages from the other stockholders who are cooperating." Bad faith was to be attributed to claimants who opposed a plan for a time until they were "bought off;" those who "refused to vote in favor of a plan unless. . . given some particular preferential advantage."

Young v. Higbee Co., 324 U.S. at 211, n.10, 65 S.Ct. at 598, n.10, 89 L.Ed. 897, n.10 (citations omitted).

The test followed by a majority of courts regarding § 1126(e) has been described as follows:

> Good faith voting does not require, nor can it expect, a creditor to act with selfless disinterest. *In re Federal Support Co.*, 859 F.2d 17, 19 (4th Cir. 1988). The test then, consonant with the United States Supreme Court's standard, is whether a creditor has cast his vote with an "ulterior purpose" aimed at gaining some advantage to which he would not otherwise be entitled in his position. *In re A.D.W., Inc.*, 90 B.R. 645, 649 (Bankr. D.N.J. 1988); *In re MacLeod Co., Inc.*, 63 B.R. 654, 655 (Bankr. S.D. Ohio 1986). Ulterior or coercive motives that have been held to constitute bad faith include "pure malice, 'strikes', blackmail, and

> the purpose to destroy an enterprise in order to advance the interests of a competing business." *In re Federal Support Co.*, 859 F.2d at 19 (citing *In re Pine Hill Collieries, Co.*, 46 F.Supp. 669, 671 (E.D.Pa. 1942).

In re Gilbert, 104 B.R. 206, 216 (Bankr. W.D. Mo. 1989);

See also In re Pleasant Hill Partners, L.P., 163 B.R. 388, 392 (Bankr. N.D. Ga. 1994); *In re Federal Support Co.*, 859 F.2d 17, 19 (4th Cir. 1988); *In re MacLeod Co., Inc.*, 63 B.R. 654, 655 (Bankr. S.D. Ohio 1986).

In the Ninth Circuit, the court, in the recent case of *In re Marin Town Center*, 142 B.R. 374, 378-79 (N.D. Cal. 1994), applying the test for good faith, stated as follows:

> The test is whether a vote is cast for the ulterior purpose of securing some advantage to which the creditor would not otherwise have been entitled. Ulterior motives which have been held to constitute bad faith include "pure malice, 'strikes,' and blackmail, and the purpose to destroy an enterprise in order to advance the interests of a competing business . . ." *In re Pine Hill Collieries, Co.*, 46 F.Supp. 669, 671 (E.D.Pa. 1942). Thus, section 1126(e) has been used to prevent minority creditors from extorting, and debtors from making preferential payments in exchange for votes; it has also been used to prevent a competitor from advancing a competing business by blocking reorganization. *See, e.g., In re MacLeod Co, Inc.*, 63 B.R. 654 (Bktcy. S.D. Ohio 1986).
>
> However, this case does not involve any of the scenarios which have been held to constitute bad faith. A vote cannot be said to have been cast in bad faith simply because it was

> voted for the purpose of blocking confirmation of a reorganization plan. In fact, rejection of a plan by "a party, largely interested in the Debtor before his acquisition of controlling rights, who withholds consent to a plan primarily because he believes its consummation will be more injurious to his investment in the Debtor than liquidation, meets the standard of good faith." *In re Pine Hill Collieries, Co.*, 46 F.Supp. at 671. Section 1126(e) does not require a creditor to have an interest in seeing the debtor reorganize. *In re Federal Support Co.*, 859 F.2d 17, 19 (4th Cir. 1988) ("Each creditor is expected to cast his vote in accordance with his perception of his own self-interest. . . .").

In analyzing the holdings by various courts regarding the test for determining good faith under § 1126(e) and its predecessor § 203, the following was presented in the treatise, "Chapter 11 Theory and Practice" edited by the Chief Bankruptcy Judge James F. Queenan, Jr.,

> There is nothing wrong with a creditor acting selfishly in the protection of his interest as a creditor, but when he votes to promote another interest, it is unfair to the other creditors who seek only to advance their interests as creditors. . . .
>
> [A] court will not disqualify the vote of a *purchased claim* if it is convinced the claimant voted out of a genuine concern to protect its interest as a [pre-existing] creditor. Judge Frank, writing for the Second Circuit, put it this way:
>
> > The mere fact that a purchase of creditors' interests is for the purpose

> of securing the approval or rejection of a plan does not of itself amount to "bad faith." When that purchase is in aid of an interest other than an interest as a creditor, such purchases may amount to "bad faith" under section 203 of the Bankruptcy Act.[420]
>
> [420] *In re P-R Holding Corp.*, 147 F.2d 895, 897 (2d Cir. 1945).

Decisions under section 203 of the Act and section 1126(e) of the Code recognize the wrong in a party voting a claim for the primary purpose of advancing a noncreditor interest. In *In re McLeod Co.*,[421] for example, the court disqualified the votes of former employees because it found the votes were motivated by a desire to destroy the debtor and thereby promote a competing business that the former employees had started.

Some of the decisions involve simpler facts. It is wrong for the vote to be motivated by an additional payment on the voted claim.[422] It is improper for a party soliciting rejection (or acceptance) of a plan to send creditors premarked ballots.[423]

[421] 63 B.R. 654, 14 BCD 915 (Bankr. S.D. Ohio 1986).

[422] *E.G., In re Featherworks Corp.*, 25 B.R. 634, 9 BCD 1320 (Bankr. E.D. N.Y. 1982), *aff'd*, 36 B.R. 460 (E.D.N.Y. 1984) (bad faith found when creditor wished to change vote after receiving payment from affiliate of debtor to drop suit against affiliate).

> [423] *In re Gulph Woods Corp.*, 83 B.R. 339, 17 BCD 257 (Bankr. E.D. Pa. 1988).
>
> The voting of purchased claims is more likely to be challenged because of the presumed existence of strong financial motives behind the purchases. But a court will not disqualify the vote of a purchased claim if it is convinced the claimant voted out of a genuine concern to protect its interest as a creditor.

5 *James F. Queenan, Jr. et al., Chapter 11 Theory and Practice: A Guide to Reorganization* §30.25, at 30:101 (1994) (insert added).

See also 5 *Collier on Bankruptcy*, ¶ 1126.05, at 1126-20 (15th ed. 1994).

In applying § 1126(e) to the instant case, the court, following the authorities cited herein, is of the view that good faith does not require, nor can it be expected, that a creditor will act with selfless disinterest. Each creditor is expected to act in accordance with his perception of his own self interest, but may not act with an ulterior or coercive purpose.

Application of the §1126(e) To The Instant Case

This court finds that Teachers, in acquiring the twenty-one unsecured claims, acted in good faith within the meaning of § 1126(e). Teachers, as a pre-existing creditor, exercising its business judgment, acted out a genuine concern to protect its own self interests. Teachers held a legitimate belief that the Debtor's Plan exposed it to significant risks not bargained for when it made the loan to the Debtor, and that the Debtor's attempt at cramdown was not in its best interest. Teachers' acquisition of the claims in question was motivated by self interests and not by an ulterior motive.

Teachers' selfish motives in attempting to defeat the Debtor's Plan does not constitute bad faith. *Gilbert*, 104 B.R. at 216; *Marin Town Center*, 142 B.R. at 379. 5 *Collier on Bankruptcy* ¶ 1126.05, at 1126-20.

The Debtor contends that this court should consider the totality of the circumstance surrounding Teachers' purchases of the unsecuted claims in question in deciding whether they were acquired in good faith, citing *In re Allegheny Intern., Inc.*, 118 B.R. 282 (Bankr. W.D. Pa. 1990). In that case, the court considered the facts and circumstances surrounding the purchases of claims, i.e., the purchaser's intent to take over the debtor; its plan proponent status; the timing of the purchases; the amount paid for the claims; the fact that the purchaser was an outsider prior to its purchase of claims; and its use of its veto power to improve its position in applying § 1126(e), concluding that the votes in question were acquired and cast in bad faith and would be disqualified. *Id.* at 289-90.

In the instant case, the court finds that considering the facts and circumstances surrounding the purchase of the claims in question, Teachers acted in good faith within the meaning of § 1126(e).

Purpose and Intent

The Debtor contends that Teachers' purchases were made in bad faith because they were not made as a part of a good faith exercise of Teachers' business judgment seeking to protect its interest as a pre-existing secured creditor. Rather, the Debtor asserts that Teachers acted in furtherance of the alleged ulterior motives of foreclosing on Skyline Terrace at all costs and eliminating the existing lender liability litigation.

Contrary to the Debtor's contentions, this court finds that Teachers acted out of a genuine concern to protect its own self-interest as a pre-existing creditor. Teachers reasonably believed that it was in its best interests to acquire Skyline Terrace to satisfy the obligation owed to it, and that there was no merit to Debtor's lender liability action. Teachers did not act to further an ulterior motive. The record is void of evidence of any pure malice or blackmail. Nor does the record support a finding that Teachers' purpose in purchasing the unsecured claims in question was part of a scheme to destroy the Debtor. Teachers, as a banking institution, was not a competitor of the Debtor, but rather a pre-existing secured creditor. The Debtor's assertions of ulterior motives are without merit.

Plan Proponent

The Debtor asserts that Teachers' conduct in acquiring the unsecured claims should be evaluated in terms of Teachers' being a plan proponent in contrast to a pre-existent creditor concerned with its own self interests.

The court finds that, in reality, Teachers was not a plan proponent when it purchased the unsecured claims in question. The fact that Teachers had not formally withdrawn its Plan until December 16, 1994, does not contribute to a finding of bad faith. Teachers' Plan was premised on the assumption that Teachers' claim was undersecured, its contention being that Skyline Terrace had a fair value of fourteen (14) million dollars. Teachers' belief that its claim was undersecured was the essence of its Plan. When, on August 24, 1994, this court determined that the fair value of Skyline Terrace was $19.3 million dollars, Teachers was no longer a competitor regarding the Debtor's Plan, as Teachers' claim was not undersecured, but rather oversecured. The

record is void of any effort by Teachers subsequent to August 24, 1994 to propose its own amended plan.

Unfair Discrimination

The Debtor contends that the effect of Teachers' purchases is to discriminate unfairly against non-selling creditors in favor of selling creditors, pointing out that selling creditors would receive one-hundred percent of their claim from Teachers, while non-selling creditors would receive only eighty percent of their claims under the Debtor's Plan.

Contrary to the Debtor's assertions, this court finds no unfair discrimination as a result of the purchase of the claims in question, as the record before this court establishes that Teachers offered to purchase all of the Class 3 unsecured claims for one-hundred cents on the dollar. Non-selling creditors had the same opportunity as selling creditors to receive one-hundred cents on the dollar. Teachers cannot be held to have acted in bad faith because certain unsecured creditors declined to accept one-hundred cents on the dollar. The instant case is distinguishable from *In re P-R Holding Corp.*, 147 F.2d 895 (2nd Cir. 1945), cited by the Debtor. In that case, the purchaser failed to offer to purchase certificates from all certificate holders, resulting in unfair discrimination in favor of the selling certificate holders. In the instant case, Teachers offered to purchase all of the unsecured claims classified in Class 3 for one-hundred cents on the dollar.

Timing and Manner

The Debtor asserts that the timing and manner whereby Teachers purchased the unsecured claims in question indicates bad faith. The Debtor contends that Teachers purchased the claims at the eleventh hour, after being thwarted in its attempts to obtain relief from stay and after it was determined that its claim was oversecured. The Debtor points out that Teachers purchased primarily the smallest amounts of the unsecured claims, concentrating its efforts on purchasing enough claims to control the number of claimants in the class, in contract to controlling the amount of the claims in the class. In addition, the Debtor contends that Teachers actively concealed the claims purchases from the Debtor.

The Debtor's assertions lack merit. This court finds that the timing and manner whereby Teachers purchased the unsecured claims in question do not indicate bad faith. At the time Teachers purchased the unsecured claims, its Plan was no longer in competition with the Debtor's Plan. Teachers acted out of a genuine concern to protect its own self-interest as a pre-existing creditor, notwithstanding its claim being oversecured and the withdrawal of its request for relief from stay. Contrary to the Debtor's assertion, Teachers did not discriminately attempt to control the number of claimants in Class 3, as it offered to purchase all of the claims classified in Class 3 at one-hundred cents on the dollars. Teachers did not conceal these acquisitions, as the offer to purchase was made to all unsecured claimants. Teachers complied with the requirements prescribed in Rule 3001(e)(2). Teachers was not obligated to inform the Debtor informally that it intended to purchase these claims prior to their acquisition by Teachers.

Conflict of Interest

The Debtor contends that bad faith exists because Teachers, as a member of a fully secure class, has an alleged conflict of interest with the Class 3 claimants, the alleged conflict resulting from its acquiring the unsecured claims in question.

This court finds that the fact that Teachers is a secured creditor under the Debtor's Plan does not represent a conflict of interests concerning its acquired unsecured claims. Teachers may vote in both classes in a manner consistent with its own self interests. This does not represent a conflict of interests. Courts have recognized that claims purchases made by a creditor holding claims in more than one class are in good faith. *See, e.g., In re Concord Square Apartments*, 174 B.R. 71, 73 (Bankr. S.D. Ohio 1994); *Pleasant Hill Partners*, 163 B.R. at 389-90; *Gilbert*, 104 B.R. at 208; *Pine Hill Collieries*, 46 F.Supp. at 670-71.

Pending Litigation

Teachers' Plan had referred to the existing litigation entitled (1) *Teachers Insurance and Annuity Association of America vs. Figter Limited, et al.*, Los Angeles Superior Court Case No. BC 078958, wherein the Debtor sued Teachers alleging that Teachers wrongfully refused to enter into a restructuring of the Debtor's obligations to Teachers, and (2) *Figter Limited vs. Teachers Insurance and Annuity Association of America, et al.*, filed in this bankruptcy court, Adversary No. LA 93-04661 AG, wherein allegations regarding lender liability were made.

Confirmation of Teachers' Plan would have resulted in the dismissal of both the federal and State court actions with prejudice. The Debtor's Plan, however,

would allow the Debtor, in its sole discretion, to discontinue or continue the prosecution of the adversary action in this bankruptcy court to a compromise, settlement or judgment.

The Debtor contends that Teachers, in acquiring the unsecured claims, acted to further the ulterior motive of eliminating the pending litigation. The Debtor's contention is without merit. Initially, it should be emphasized that the pendency of a lawsuit against a creditor does not of itself constitute grounds for finding a lack of good faith under § 1126(e). *In re Federal Support Co.*, 859 F.2d 17, 20 (4th Cir. 1988); *In re A.D.W., Inc.*, 90 B.R. 645, 651 (Bankr. D. N.J. 1988); *In re Landau Boat Co.*, 8 B.R. 432, 436 (Bankr. W.D. Mo. 1981). In addition, on the date Teachers acquired the claims, Teachers was no longer pursuing the confirmation of its Plan. The dismissal of the federal and State court litigation based upon the confirmation of Teachers' Plan was no longer a reality. Also, the potential inability of the Debtor to confirm its Plan because of Teachers' acquisition of the unsecured claims would not eliminate the State court litigation.

Single Asset Real Estate Case

Contrary to the Debtor's view, the fact that the instant case involves a single real estate asset has little significance in applying § 1126(e). *See In re Concord Square Apartments*, 174 B.R., 71, 74-75 (Bankr. S.D. Ohio 1994); *In re Pleasant Hill Partners, L.P.*, 163 B.R. 388, 395 (Bankr. N.D. Ga. 1994); *In re Marin Town Center*, 142 B.R. 394, 379 (N.D. Cal. 1992).

Teachers Is Entitled To One Vote For Each Of Its Purchased Unsecured Class 3 Claims

The Debtor contends that if the court finds that the claims purchased by Teachers meets the good faith requirements of § 1126(e), Teachers should be limited to one vote for all twenty-one purchases under § 1126(c).

Section 1126(c) provides as follows:

> A class of claims has accepted a plan if such plan has been accepted by creditors, other than any entity designated under subsection (e) of this section, that hold at least two-thirds in amount and more than one-half in number of the *allowed claims of such class* held by creditors, other than any entity designated under subsection (e) of this Section, that have accepted or rejected such a plan.

Section 101(5) of the Bankruptcy Code defines a claim as a "right to payment." Section 101(10) defines creditor as an "entity that has a claim against the debtor that arose at the time of or before the order for relief."

The question before this court is whether a creditor that purchases multiple claims is entitled to a vote for each claim purchased. The courts that have addressed this question have looked to the plain language stated in 1126(c) and have determined that a purchaser of claims is entitled to a vote for each separate claim it holds. *See In re Concord Square Apartments*, 174 B.R. 71, 74-75 (Bankr. S.D. Ohio 1994); *In re Gilbert*, 104 B.R. 206, 211 (Bankr. W.D. Mo. 1989).

In the *Concord Square* case, the court, in pertinent part, stated:

> The court finds that a purchaser of claims is entitled to a vote for each separate claim it holds. This conclusion is supported by 11

> U.S.C. § 1126(c), which states: "A class of claims has accepted a plan if such plan has been accepted by creditors, . . . , that hold at least two-thirds in amount and more than one-half in number of the *allowed claims* of such class held by creditors, . . . that have accepted or rejected such plan." (emphasis added) The language distinguishes between claim-holders and claims. "The formula contained in § 1126(e) speaks in terms of the number of claims, not the number of creditors, that actually vote for or against the plan." *In re Gilbert*, 104 B.R. 206, 210 (Bankr. W.D. Mo. 1989). Thus, a creditor such as Ottawa, which holds multiple claims, has a voting right for each claim it holds."

Id. at 74.

In a similar holding, the court in the *Gilbert* case stated in pertinent part:

> The formula contained in Section 1126(c) speaks in terms of the number of claims, not the number of creditors, that actually vote for or against the plan. *In re Jeppson*, 66 B.R. 269, 294 (Bankr.D.Utah 1986); *see also, In re Jartran*, 44 B.R. 331, 364 (Bankr.N.D.Ill. 1984) (Referring to number of ballots received based on the "amount of claims voted"). The separateness of Stulz' two claims and his entitlement to two votes is not the result of any legal fiction or product of some form of bifurcation as the United States suggests. Each claim arose out of a separate transaction, evidencing separate obligations for which separate proofs of claim were filed. Votes of acceptance, such as those cast by Stulz, are to be computed only on the basis of filed and allowed proofs of

> claim. *Avery v. Fischer*, 360 F.2d 719, 725 (5th Cir. 1966) (citing 6 Collier on Bankruptcy 7.36, p. 2099 (14th ed. 1964)). Section 101(4) defines a "claim" as a "right to payment." Stulz acquired two distinct rights to payment through two separate and unrelated arms length transactions.

Id. at 211.

This court concludes that Teachers, as a good faith purchaser of twenty-one unsecured claims, is entitled to a separate vote for each claim for the reasons set in the *Concord Square* and *Gilbert* cases, as herein stated.

The post-bankruptcy cases of *In re Gilbert*, 115 B.R. 458 (Bankr. S.D. N.Y. 1990) and *In re Averil, Inc.*, 33 B.R. 562 (Bankr. S.D. Fla. 1993) cited by the Debtor, are not applicable. These cases presented the question of whether an involuntary bankruptcy case should be dis- missed for failure to meet the requirement prescribed in § 303(b)(1) that an involuntary petition be filed "by three or more entities, each of which is a holder of a claim." In the *Gilbert* case, the court held that for purposes of determining the number of entities filing an involuntary claim, an entity is considered one regardless of the number of claims it may hold. In the *Averil* case, the court held that joint payees on one promissory note constituted one entity for purposes of § 303(b)(1). Both these cases were concerned about the counting of entities under § 303(b)(1), whereas § 1126(c) counts allowed claims.

Also, the Debtor's reference to the pre-code cases of *In re Messengill*, 113 F. 366, 367 (E.D. N.C. 1902) and *In re Frank*, 9 Fed. Cas. 704, 705 (N.D. N.Y. 1871), are not applicable as well. Both cases were decided under the Bankruptcy Acts of 1867 and 1898, wherein reference was made to creditors and not claims.

DATED: May 3, 1995.

/s/ ARTHUR M. GREENWALD
ARTHUR M. GREENWALD
United States Bankruptcy Judge

APPENDIX D

11 USC § 1126

§ 1126. Acceptance of plan.

(a) The holder of a claim or interest allowed under section 502 of this title may accept or reject a plan. If the United States is a creditor or equity security holder, the Secretary of the Treasury may accept or reject the plan on behalf of the United States.

(b) For the purposes of subsections (c) and (d) of this section, a holder of a claim or interest that has accepted or rejected the plan before the commencement of the case under this title is deemed to have accepted or rejected such plan, as the case may be, if —

(1) the solicitation of such acceptance or rejection was in compliance with any applicable nonbankruptcy law, rule, or regulation governing the adequacy of disclosure in connection with such solicitation; or

(2) if there is not any such law, rule, or regulation, such acceptance or rejection was solicited after disclosure to such holder of adequate information, as defined in section 1125(a) of this title.

(c) A class of claims has accepted a plan if such plan has been accepted by creditors, other than any entity designated under subsection (e) of this section, that hold at least two-thirds in amount and more than one-half in number of the allowed claims of such class held by creditors, other than any entity designated under subsection (e) of this section, that have accepted or rejected such plan.

(d) A class of interests has accepted a plan if such plan has been accepted by holders of such interests, other than any entity designated under subsection (e) of this section, that hold at least two-thirds in amount of the allowed interests of such class held by holders of such

interests, other than any entity designated under subsection (e) of this section, that have accepted or rejected such plan.

(e) On request of a party in interest, and after notice and a hearing, the court may designate any entity whose acceptance or rejection of such plan was not in good faith, or was not solicited or procured in good faith or in accordance with the provisions of this title.

(f) Notwithstanding any other provision of this section, a class that is not impaired under a plan, and each holder of a claim or interest of such class, are conclusively presumed to have accepted the plan, and solicitation of acceptances with respect to such class from the holders of claims or interests of such class is not required.

(g) Notwithstanding any other provision of this section, a class is deemed not to have accepted a plan if such plan provides that the claims or interests of such class do not entitle the holders of such claims or interests to receive or retain any property under the plan on account of such claims or interests.

11 USC § 1129

§ 1129. Confirmation of plan.

(a) The court shall confirm a plan only if all of the following requirements are met:

(1) The plan complies with the applicable provisions of this title.

(2) The proponent of the plan complies with the applicable provisions of this title.

(3) The plan has been proposed in good faith and not by any means forbidden by law.

(4) Any payment made or to be made by the proponent, by the debtor, or by a person issuing securities or acquiring property under the plan, for services or for costs and expenses in or in connection with the case, or in connection with the plan and incident to the case, has been approved by, or is subject to the approval of, the court as reasonable.

(5)(A)(i) The proponent of the plan has disclosed the identity and affiliations of any individual proposed to serve, after confirmation of the plan, as a director, officer, or voting trustee of the debtor, an affiliate of the debtor participating in a joint plan with the debtor, or a successor to the debtor under the plan; and

(ii) the appointment to, or continuance in, such office of such individual, is consistent with the interests of creditors and equity security holders and with public policy; and

(B) the proponent of the plan has disclosed the identity of any insider that will be employed or retained by the reorganized debtor, and the nature of any compensation for such insider.

(6) Any governmental regulatory commission with jurisdiction, after confirmation of the plan,

over the rates of the debtor has approved any rate change provided for in the plan, or such rate change is expressly conditioned on such approval.

(7) With respect to each impaired class of claims or interests —

(A) each holder of a claim or interest of such class —

(i) has accepted the plan; or

(ii) will receive or retain under the plan on account of such claim or interest property of a value, as of the effective date of the plan, that is not less than the amount that such holder would so receive or retain if the debtor were liquidated under chapter 7 of this title on such date; or

(B) if section 1111(b)(2) of this title applies to the claims of such class, each holder of a claim of such class will receive or retain under the plan on account of such claim property of a value, as of the effective date of the plan, that is not less than the value of such holder's interest in the estate's interest in the property that secures such claims.

(8) With respect to each class of claims or interests —

(A) such has accepted the plan; or

(B) such class is not impaired under the plan.

(9) Except to the extent that the holder of a particular claim has agreed to a different treatment of such claim, the plan provides that —

(A) with respect to a claim of a kind specified in section 507(a)(1) or 507(a)(2) of this title, on the effective date of the plan, the holder of such claim will receive on account of such claim cash equal to the allowed amount of such claim;

(B) with respect to a class of claims of a kind specified in section 507(a)(3), 507(a)(4), 507(a)(5) or 507(a)(6), *or 507(a)(7)* of this title, each holder of a claim of such class will receive—

(i) if such class has accepted the plan, deferred cash payments of a value, as of the effective date of the plan, equal to the allowed amount of such claim; or

(ii) if such class has not accepted the plan, cash on the effective date of the plan equal to the allowed amount of such claim; and

(C) with respect to a claim of a kind specified in section ~~507(a)(7)~~ *507(a)(8)* of this title, the holder of such claim will receive on account of such claim deferred cash payments, over a period not exceeding six years after the date of assessment of such claim, of a value, as of the effective date of the plan, equal to the allowed amount of such claim.

(10) If a class of claims is impaired under the plan, at least one class of claims that is impaired under the plan has accepted the plan, determined without including any acceptance of the plan by any insider.

(11) Confirmation of the plan is not likely to be followed by the liquidation, or the need for further financial reorganization, of the debtor or any successor to the debtor under the plan, unless such liquidation or reorganization is proposed in the plan.

(12) All fees payable under section 1930 *of title 28*, as determined by the court at the hearing on confirmation of the plan, have been paid or the plan provides for the payment of all such fees on the effective date of the plan.

(13) The plan provides for the continuation after its effective date of payment of all retiree

benefits, as that term is defined in section 1114 of this title, at the level established pursuant to subsection (e)(1)(B) or (g) of section 1114 of this title, at any time prior to confirmation of the plan, for the duration of the period the debtor has obligated itself to provide such benefits.

(b)(1) Notwithstanding section 510(a) of this title, if all of the applicable requirements of subsection (a) of this section other than paragraph (8) are met with respect to a plan, the court, on request of the proponent of the plan, shall confirm the plan notwithstanding the requirements of such paragraph if the plan does not discriminate unfairly, and is fair and equitable, with respect to each class of claims or interests that is impaired under, and has not accepted, the plan.

(2) For the purpose of this subsection, the condition that a plan be fair and equitable with respect to a class includes the following requirements:

(A) With respect to a class of secured claims, the plan provides—

(i)(I) that the holders of such claims retain the liens securing such claims, whether the property subject to such liens is retained by the debtor or transferred to another entity, to the extent of the allowed amount of such claims; and

(II) that each holder of a claim of such class receive on account of such claim deferred cash payments totaling at least the allowed amount of such claim, of a value, as of the effective date of the plan, of at least the value of such holder's interest in the estate's interest in such property;

(ii) for the sale, subject to section 363(k) of this title, of any property that is subject to the liens securing such claims, free and clear of such liens, with such liens to attach to the proceeds of such sale, and the treatment of such liens on proceeds under clause (i) or (iii) of this sub-paragraph; or

(iii) for the realization by such holders of the indubitable equivalent of such claims.

(B) With respect to a class of unsecured claims—

(i) the plan provides that each holder of a claim of such class receive or retain on account of such claim property of a value, as of the effective date of the plan, equal to the allowed amount of such clai ; or

(ii) the holder of any claim or interest that is junior to the claims of such class will not receive or retain under the plan on account of such junior claim or interest any property.

(C) With respect to a class of interests—

(i) the plan provides that each holder of an interest of such class receive or retain on account of such interest property of a value, as of the effective date of the plan, equal to the greatest of the allowed amount of any fixed liquidation preference to which such holder is entitled, any fixed redemption price to which such holder is entitled, or the value of such interest; or

(ii) the holder of any interest that is junior to the interests of such class will not receive or retain under the plan on account of such junior interest any property.

(c) Notwithstanding subsections (a) and (b) of this section and except as provided in section 1127(b) of this title, the court may confirm only one plan, unless the order of confirmation in the case has been revoked under section 1144 of this title. If the requirements of subsections (a) and (b) of this section are met with respect to more than one plan, the court shall consider the preferences of creditors and equity security holders in determining which plan to confirm.

(d) Notwithstanding any other provision of this section, on request of a party in interest that is a governmental unit, the court may not confirm a plan if the principal purpose of the plan is the avoidance of taxes or the avoidance of the application of section 5 of the Securities Act of 1933 ~~(15 USC 77e)~~. In any hearing under this subsection, the governmental unit has the burden of proof on the issue of avoidance.

No. 97-546

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In The

Supreme Court of the United States

October Term, 1997

FIGTER LIMITED,

Petitioner,

vs.

TEACHERS INSURANCE AND ANNUITY ASSOCIATION OF AMERICA,

Respondent.

ON PETITION FOR WRIT OF CERTIORARI
TO THE UNITED STATES COURT OF APPEALS
FOR THE NINTH CIRCUIT

RESPONDENT'S OPPOSITION TO PETITION FOR WRIT OF CERTIORARI

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TO THE HONORABLE SUPREME COURT:

Respondent, Teachers Insurance and Annuity Association of America ("Teachers"), submits this brief in opposition to the petition for a writ of certiorari submitted by Petitioner, Figter Limited (the "Debtor").

INTRODUCTION

The Ninth Circuit Court of Appeal's decision, Figter Ltd. v. Teachers Insurance and Annuity of Association of America (In re Figter Ltd.), 118 F.3d 635 (9th Cir. 1997), attached as Appendix A to the petition, involves the interpretation of §§ 1126(c) and 1126(e) of the Bankruptcy Code and the application of those provisions to the situation where an oversecured creditor (Teachers), who is a pre-existing creditor and not a competitor of the debtor nor a plan proponent, purchases unsecured claims by offering to purchase all non-insider unsecured claims for one-hundred cents on the dollar with the intent of blocking confirmation of the debtor's plan which it legitimately believes is not in its best interests.

The Ninth Circuit Court of Appeals concluded that the bankruptcy court did not err in either its factual or legal determinations that Teachers' acquisition of the unsecured claims was made in "good faith" within the meaning of § 1126(e) and that Teachers should be entitled, pursuant to § 1126(c), to one vote per purchased claim.

Because Figter does not conflict with a decision of another court of appeals, does not decide a federal question in a way that conflicts with applicable decisions of this Court, and does not decide an important question of federal law which has not been, but should be, settled by this Court, this Court should deny the Debtor's petition for writ of certiorari.

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STATEMENT OF THE CASE

The Debtor filed a voluntary petition on May 27, 1993. (Petitioner's Appendix ("App.") C, 3.) The Debtor's primary asset is a 198-unit multi-family residential apartment complex (Skyline Terrace) located in downtown Los Angeles (the "Property"). (App. C, 5.) Teachers is a pre-existing creditor by virtue of a $15.6 million promissory note, executed by the Debtor in favor of Teachers on April 29, 1989, and secured by a first trust deed lien on the Property. (App. C, 5.)

The Debtor's plan of reorganization, filed on December 23, 1993, (the "Plan") proposes to convert the Skyline Terrace into condominiums, with a sales program of approximately three years, and with Teachers to release portions of its lien as individual condominiums are sold. (App. C, 6.)

The Plan classifies Teachers' secured claim in Class 2 and classifies the unsecured claims in Class 3. Class 2 and Class 3 were the only impaired classes. (App. C, 6.)

Because Teachers would not vote to approve the Plan, Class 3 represented the only potential consenting impaired class.

During the period October 27, 1994 through October 31, 1994, Teachers offered to purchase *all* of the Class 3 unsecured claims for *one-hundred cents on the dollar*. (App. C., 8, 19, and 20.) During this period, Teachers purchased twenty-one of the thirty-six unsecured claims classified in Class 3 at one-hundred cents on the dollar for a total of $14,588.62. (App C, 8.) On or about November 23, 1994, Teachers filed with the Clerk of the Bankruptcy Court Notices of Transfer of Claim as required by Rule 300(1)(e)(2) of the Federal Rules of Bankruptcy Procedure. (App. C, 8 and 20.) On or about December 14, 1994, the Clerk of the Court served its Notice of Transfer of Claims on Teachers, the transferors, and the Debtor. (App. C, 8.) No objection was filed by any transferor within the twenty-day period provided for in Rule 3001(e)(2). (Id.)

Teachers was not a plan proponent when it purchased the claims. (App. C, 18, 20, and 22.) When, on August 24, 1994, the bankruptcy court determined that Teachers was oversecured, Teachers, whose plan was premised on the belief that Teachers' claim was undersecured (App. C, 7 and 18), was no longer a competitor regarding the Debtor's plan. (App. C, 18.) The record is void of any effort by Teachers subsequent to August 24, 1994 to propose its own amended plan. (App. C, 8 and 18-19.) Thus, at the time Teachers purchased the claims, its plan was no longer in competition with the Plan. Accordingly, the Debtor's assertion that "the secured creditor was a plan proponent at the time it made the purchases" (Petition, 13) is a misstatement of fact.

If Teachers is allowed to vote each of the claims it purchased, the Plan will be unconfirmable on its face, as the Debtor will be unable to meet the requirements of 11 U.S.C. § 1129(a)(10), i.e., the existence of an impaired consenting class of claims, and, therefore, the Debtor will be unable to cramdown Teachers' secured claim under § 1129(b). (App. C, 5.)

Teachers' acquisition of the claims, made with the intent of rendering the Plan unconfirmable, was not motivated by an ulterior or coercive motive (App. C, 16 and 18): (1) the record is void of any evidence of any pure malice or blackmail (App. C, 18); (2) the record does not support a finding that Teachers' acquisition of the claims was part of a scheme to destroy the Debtor since Teachers is not a competitor of the Debtor (Id.); and (3) the inability of the Debtor to confirm a plan will not eliminate pending state court lender liability action brought by the Debtor against Teachers, which action is based on the Debtor's allegations that Teachers wrongfully refused to enter into a restructuring of the Debtor's obligations to Teachers (App. C, 22).

Instead, Teachers was motivated by a genuine concern to protect its own self interests as a pre-existing creditor: Teachers holds a legitimate belief that the Plan, if confirmed, would expose it to significant risks not bargained for when it made the loan to the Debtor and that, therefore, the Debtor's attempt to cramdown its secured claim is not in Teachers' best interests. (App. C, 16, 18, ,19, and 20.)

These factual findings, entered by the Bankruptcy Court and affirmed by both the District Court and the Court

of Appeals, should not be unsettled by this Court. See Goodman v. Lukens Steel Co., 482 U.S. 656, 665 (1987).

ARGUMENTS FOR DENYING THE PETITION

A. The Ninth Circuit Court Of Appeals, In Figter, Did Not Enter A Decision In Conflict With A Decision Of Another Court Of Appeals.

Figter does not conflict with a decision of another court of appeals. The Debtor does not suggest otherwise.

B. The Ninth Circuit Court Of Appeals, In Figter, Did Not Decide A Federal Question In A Way That Conflicts With Applicable Decisions Of The Supreme Court.

1. The Ninth Circuit Court of Appeals' interpretation of § 1126(e) does not conflict with any applicable decision of the Supreme Court.

Contrary to the Debtor's assertions, Figter, in interpreting "good faith" within the meaning of § 1126(e) to include purchases of unsecured claims by an oversecured creditor with the intent to block confirmation of a plan, does not conflict with Pioneer Investment Services Co. v. Brunswick Assoc. L.P., 507 U.S. 380, 389 (1993) or Young v. Higbee, 324 U.S. 204, 210-11 (1945).

First, Pioneer Investments is not applicable. Pioneer Investments does not hold, let alone state, that a court must interpret language left undefined by Congress in the Bankruptcy Code (e.g., "good faith" in § 1126(e)) in a manner that insures that a debtor will successfully reorganize. Pioneer Investments merely describes a bankruptcy court's general equitable powers:

> bankruptcy courts are entrusted with broad equitable powers to balance the interests of the affected parties, guided by the overriding goal of insuring the success of the reorganization.

507 U.S. at 389. As this Court makes clear in Norwest Bank Worthington v. Ahlers, 485 U.S. 197, 207 (1988), a bankruptcy court's equitable powers can only be exercised within the confines of the Bankruptcy Code and cannot be used to interpret the Code with a debtor's green glasses:

> whatever equitable powers remain in the bankruptcy courts must and can only be exercised within the confines of the Bankruptcy Code. . . . The Court of Appeals may well have believed that [the Lender] or other unsecured creditors would be better off if [the debtors'] reorganization plan was confirmed. But the determination is for the creditors to make in the manner specified by the Code. 11 U.S.C. § 1126(c).

Because Figter involves the interpretation of the Bankruptcy Code and not a bankruptcy court's exercise of its equitable powers, Pioneer Investments is not applicable.

Second, the Ninth Circuit Court of Appeals' interpretation of § 1126(e) does not conflict with Young. This Court, in Young, in discussing § 203 of the Bankruptcy Act, the predecessor to § 1126(e), did not hold that a creditor's acquisition of claims to block confirmation of a plan is not "good faith." Instead, this Court explained that this provision was intended to apply to those

> whose selfish purpose was to obstruct a fair and feasible reorganization in the hope that someone would pay them more than the ratable equivalent of their proportionate part of the bankrupt assets.

324 U.S. at 211 (emphasis added). This Court further elucidated the legislative history of § 203 in footnote 10:

> A year before the House Committee on the Judiciary held its extensive hearings on the Chandler Act a Circuit Court of Appeals held that a creditor could not be denied the privilege of voting on a reorganization plan under Sec. 77B, although he bought the votes for the purpose of preventing confirmation unless certain demands of his should be met. Texas Hotel Corporation v. Waco Development Co., 5 Cir., 87 F.2d 395. The hearings make clear the purpose of the Committee to pass legis-

> lation which would bar creditors from a vote who were prompted by such a purpose. To this end they adopted the 'good faith' provisions of Sec. 203. Its purpose was to prevent creditors from participating who 'by the use of obstructive tactics and hold-up techniques exact for themselves undue advantages from the other stockholders who are cooperating.' Bad faith was to be attributed to claimants who opposed a plan for a time until they were 'bought off'; those who 'refused to vote in favor of a plan unless . . . given some particular preferential advantage.' Hearings on Revision of the Bankruptcy Act before the Committee on the Judiciary of the House of Representatives, 75th Cong., 1st Sess. on H.R. 6439, Serial 9, pp. 180-182.

The Ninth Circuit Court of Appeals, in interpreting § 1126(e) to mean that a creditor's purchases of claims are made in "good faith" when the purchases are made with the motivation of protecting the creditor's economic interests as a pre-existing creditor as opposed to an ulterior motive such as blackmail, strike, or malice, is entirely consistent with Young. Indeed, Figter consistently follows Young and the line of cases which, with the guidance of Young, have interpreted § 1126(e). (App. A, 5-7) (following Young and the line of cases interpreting § 1126(e) with the guidance of Young: 255 Park Plaza Associates Ltd. Partnership v. Connecticut General Life Ins. Co. (In re 255 Park Plaza Associates, Ltd. Partnership), 100 F.3d 1214, 1219 (6th Cir. 1996); Insinger Machine Co. v. Federal Support Co. (In re

Federal Support Co.), 859 F.2d 17, 19 (4th Cir. 1988); In re Marin Tower Ctr., 142 B.R. 374, 378-79 (N.D. Cal. 1992); In re Holly Knoll Partnership, 167 B.R. 381, 385-86 n. 4 (Bankr. E.D. Pa. 1994); In re Landing Associates, Ltd., 157 B.R. 791, 803 (Bankr. W.D. Tex. 1993); In re Applegate Property, Ltd., 133 B.R. 827, 834 (Bankr. W.D. Tex. 1991); In re Allegheny International, Inc., 118 B.R. 282, 288-89 (Bankr. W.D. Pa. 1990); In re Gilbert, 104 B.R. 206, 215-16 (Bankr. W.D. Mo. 1989); In re A.D.W., Inc., 90 B.R. 645, 648 (Bankr. D. N.J. 1988); In re MacLeod Co., 63 B.R. 654, 655 (Bankr. S.D. Ohio 1986); In re Landau Boat Co., 8 B.R. 432, 433-34 (Bankr. W.D. Mo. 1981)).

2. The Ninth Circuit Court of Appeals' interpretation of § 1126(c) does not conflict with any applicable decision of the Supreme Court.

The Ninth Circuit Court of Appeals, in Figter, interpreted § 1126(c) to mean that a creditor is entitled to one vote for each of its purchased claims, which interpretation is supported by the two other decisions that have addressed this issue: In re Concord Square Apartments, 174 B.R. 71, 74-75 (Bankr. S.D. Ohio 1994), and In re Gilbert, 104 B.R. at 211. The Ninth Circuit Court of Appeals' conclusion is based on the plain language of § 1126(c) which states that "claims" and not "creditors" are counted:

> [a] class of claims has accepted a plan if such plan has been accepted by creditors, other than any entity designated under subsection (e) of this section, that hold at least two-thirds in

> amount and more than one-half in number of the allowed claims of such class held by creditors, other than any entity designated under subsection (e) of this Section, that have accepted or rejected such a plan. [Emphasis added.]

Because the language of § 1126(c) is not ambiguous, and because, in any event, the old law to which the Debtor refers is either inconsistent with the language of § 1126(c) or not relevant to the issue of counting claims for the purpose of accepting or rejecting a plan, Dewsnup v. Timm, 502 U.S. 410 (1992), is not applicable. The Ninth Circuit correctly so reasoned. (App. A, 9-10.) Indeed, to do otherwise would run afoul of this Court's dictate in United States v. Ron Pair Enterprises, 489 U.S. 235, 241 (1989) that "judicial inquiry is complete" when the words of a statute are unambiguous.

C. The Ninth Circuit Court Of Appeals, In Figter, Did Not Decide An Important Question Of Federal Law Which Has Not Been, But Should Be, Settled By The Supreme Court.

The Bankruptcy Code represents Congress' delicate balance of the rights of debtors and the rights of creditors, which balance this Court should not upset. See Beezley v. California Title Co. (In re Beezley), 994 F.2d 1433, 1439-40 (9th Cir. 1992) (O'Scannlain, J., concurring). A creditor's ability to purchase claims, and the concomitant ability of a creditor to sell its claim, further the creditor control principle embodied by the Bankruptcy Code and recognized by this Court. See Phoenix Mutual Life Ins. Co. v. Greystone III

Joint Venture (In re Greystone III Joint Venture), 995 F.2d 1274, 1283 (5th Cir. 1991) (citing Ahlers, 485 U.S. at 206). Indeed, where, as here, the secured creditor offers to purchase all of the claims of noninsider creditors for one-hundred cents on the dollar, all noninsider creditors benefit. This situation is not the "free-for-all" feared by the bankruptcy court in Applegate where creditors will not be paid equally, where fraud and corruption will be invited, and where a creditor will purchase claims in exchange for forbearance in potential violation of the federal securities laws. Instead, it affords every noninsider creditor of the debtor the option of having their claims paid in full.

Congress embued this creditor control principle in § 1126(e), which, as elucidated by the legislative history and the relevant and unanimous case law, makes it clear that a creditor, such as Teachers, acts in good faith when it purchases claims to preclude confirmation of a plan when its action is motivated by a desire to protect its economic interests as a pre-existing creditor and not by an ulterior purpose. Even though a creditor's ability to vote claims that it purchased often frustrates the efforts of a debtor, especially a single asset real estate debtor, to successfully reorganize, the Debtor's concern is one that the Debtor should raise with Congress and not this Court. If such purchases risk the loss of a debtor's equity through liquidation or foreclosure, the solution may be found in the economics of the marketplace, e.g., obtaining alternate financing, not in the judicial rewriting of the Bankruptcy Code.

CONCLUSION

For the foregoing reasons, the petition for writ of certiorari does not present a compelling reason for this Court to grant certiorari. Respondent respectfully requests this Court to deny the petition.

Dated: October 29, 1997

Respectfully submitted,

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PETITIONER'S REPLY BRIEF

INTRODUCTION

Petitioner Figter Limited ("Figter") respectfully submits this Reply Brief in further support of its Petition for a Writ of Certiorari and in reply to the Opposition to the Petition filed by Respondent Teachers Insurance and Annuity Association of America ("TIAA"). The Petition arises in the context of Petitioner Figter's Chapter 11 bankruptcy case and from the purchases by Respondent TIAA of twenty-one claims in the unsecured class in which it was previously not a member. Respondent has admitted that its purpose in purchasing the unsecured claims was to block the Petitioner's plan of reorganization. The Court of Appeals for the Ninth Circuit affirmed the decisions of the District and Bankruptcy Courts below holding that the purchased claims would not be designated as being purchased in bad faith and that Respondent could cast one vote for each of the purchased claims. The Petitioner seeks review of the Ninth Circuit Opinion not only because such decision conflicts with applicable Supreme Court precedent, but because the decision below raises important Federal questions regarding the purpose, policies and operation of the Bankruptcy Code and the impact on Chapter 11 debtors and their ability to reorganize.

In the Petition, the Petitioner demonstrated that, contrary to arguments set forth in Respondent's Opposition Brief, that the opinion below ***does*** conflict with applicable Supreme Court precedent (Petition at 6-8) and that the Federal questions raised ***are*** important ones (Petition at 8-12). The Petition should be granted so that this Court may settle these important Federal questions.

1. The Ninth Circuit Opinion Decided Important Questions of Federal Law Which Should Be Settled by this Court.

In its Opposition, Respondent asserts that the Ninth Circuit did not decide an important Federal question. (Resp. Br. at 10). Respondent does not, however, discuss why the issues determined by the Court of Appeals are not important questions of Federal law. Respondent argues that the Bankruptcy Code "represents Congress' delicate balance of the rights of debtors and the rights of creditors" (Resp. Br. at 10), but does not explain what that balance is and what impact the Ninth Circuit's Opinion has on such "balance." More significantly, Respondent failed to address any of the Petitioner's arguments in the Petition regarding the impact and effect of the Ninth Circuit Opinion on the Bankruptcy Code and its purposes, on Chapter 11 debtors and on single asset real estate cases.

As discussed in the Petition, the Ninth Circuit Opinion would permit any secured creditor in a Chapter 11 case to purchase a blocking position so as to prevent a Chapter 11 debtor from meeting the requirements of Section 1129 of the Bankruptcy Code and thereby to have a plan of reorganization confirmed. If the Federal courts were to sanction such activity, it would have the practical and adverse effect of preventing any reorganization in a Chapter 11 case where the secured creditor decided to engage in such tactics. The impact of the Ninth Circuit Opinion would thus not be limited to the particular facts of this case. Its impact would be seen in variety of circumstances, involving any Chapter 11 debtor and a secured creditor or creditors in such a case. The consequence of the Ninth Circuit Opinion would thus severely undermine the operation and purposes of the Code.

To allow the purchase of a blocking position by a fully-secured creditor, especially where it previously held no unsecured claim which it could argue it was trying to protect,

would, in effect, sound the death knell for virtually all Chapter 11 cases. In every case, the secured creditor could simply purchase either 51% in number or over one-third in amount of the unsecured claims and thereby be virtually assured of being able to block the confirmation of a cramdown plan by the debtor. This cannot be the result which Congress intended. Indeed, it is submitted that such activity is the very type of harm which Congress sought to empower and direct the Bankruptcy Courts to prevent when it enacted Section 1126(e).

Contrary to Respondent's assertions, the Ninth Circuit Opinion will result in a "free for all" whereby a secured creditor will attempt, as in the case at bar, to buy as many claims as possible to obtain a blocking position ***before*** any plan has been proposed and ***before*** any Court-approved disclosure statement has been transmitted to creditors so that they have adequate information prior to determining whether to sell their claims, all in contravention of the disclosure and solicitation provisions of the Code. A secured creditor can acquire its blocking position without adhering to the strictures of Section 1125. This would upset the "delicate balance" enacted by Congress (and alluded to by Respondent) as set forth in Sections 1125 (providing for a Court-approved disclosure statement to be used in soliciting acceptances of a plan), 1126 (setting forth voting procedures on a plan) and 1129 (setting forth confirmation requirements) of the Code. The designation of the claims purchased by Respondent as nonvoting will preserve the primary purpose of Chapter 11 and prevent the type of abuse by secured creditors in Chapter 11 cases in which Respondent has engaged.

Indeed, Respondent's tactic in purchasing claims to block confirmation of a debtor's plan is not and cannot be an isolated case. It would be a rare debtor, however, which would have the resources and opportunity to seek review by this Court of the pernicious conduct engaged in here. The

fact that such claims trading may result in blocking the successful reorganization of a Chapter 11 debtor does not mean that such conduct and its adverse consequences to the purposes and policies underlying the Code should be insulated from review by this Court. This case provides the opportunity for the Court to undertake such review.

As discussed, the Ninth Circuit Opinion adversely affects all Chapter 11 cases. Single-asset debtors, such as the Petitioner, however, are particularly susceptible and vulnerable to a secured creditor engaging in claims purchasing because such debtors typically have only one single, secured creditor and a number of unsecured trade creditors. The sole secured creditor in such a situation may more easily acquire a blocking position. This adverse impact on single-asset debtors also warrants review of the Ninth Circuit Opinion by this Court.

As discussed in the Petition (at 11-12), the Code was most recently amended by Congress in 1994. Pub. L. 103-94, 108 Stat. 4106 (1994). Significantly, as noted by various commentators, the 1994 amendments did ***not*** bar single-asset debtors from seeking Federal bankruptcy protection. If Congress had intended that single asset debtors would not be entitled to reorganize under Chapter 11, it could have done so by way of the 1994 amendments. It chose not to do so. Judicial interpretations of the Code, such as set forth in the Ninth Circuit Opinion, which render it difficult or impossible for a single asset real estate debtor such as the Petitioner to reorganize, are inconsistent with the purpose and policy of the Code and the intent of Congress.

The Ninth Circuit Opinion thus involves important Federal questions warranting review by this Court.

2. The Ninth Circuit Opinion Conflicts with Supreme Court Precedent.

Respondent's argument that *Pioneer Investment Services Co. v. Brunswick Assoc. LP*, 507 U.S. 380 (1993), is inapplicable to this case is without merit. Respondent concedes that the meaning of "good faith" for purposes of Section 1126(e) of the Bankruptcy Code was left undefined by Congress (Resp. Br. at 6). The Bankruptcy Courts are thus left with the discretion, in the exercise of their equitable powers, to interpret the meaning of such term. As the Petitioner stated in the Petition, in *Pioneer*, this Court stated that "bankruptcy courts are entrusted with broad equitable powers *to balance the interests of the affected parties, guided by the overriding goal of insuring the success of the reorganization.*" 507 U.S. at 389 (emphasis added). Although the Petitioner agrees with Respondent that the Bankruptcy Code need not be interpreted with a "debtor's green glasses," *Pioneer* does require that the Bankruptcy Courts "*balance the interests of the affected parties.*" *Id.* It would appear that, at the very least, *Pioneer* requires that, in the absence of the expression of any legislative intent to the contrary, in exercising their equitable powers in balancing such interests (for example in interpreting the provisions of the Code as Congress entrusted such Courts to do), the Bankruptcy Courts should err on the side of promoting a successful reorganization. In interpreting "good faith" under Section 1126(e) of the Code in a manner which renders it difficult, if not impossible, for the Petitioner to reorganize, the Ninth Circuit Opinion was clearly not guided by the "*overriding goal of insuring the success of the reorganization.*"

Also without merit is Respondent's argument that this Court's decision in *Young v. Higbee*, 324 U.S. 204 (1945), which interpreted the predecessor statute to Section 1126(e) of the Code (Section 203 of the Bankruptcy Act of 1898, 11 U.S.C. § 603), was ***only*** intended to apply to those whose

selfish purpose was "to obstruct a fair and feasible reorganization in the hope that someone would pay them more than the ratable equivalent of their proportionate part of the bankrupt assets." 324 U.S. at 210-211. In fact, various Federal courts, following *Young*, have found bad faith within the meaning of Section 1126(e) of the Code in a variety of circumstances and not just where the creditor obtained a plan blocking position for the limited purpose of obtaining more than its fair share of any distribution. *See, e.g., In re Applegate Property, Ltd.*, 133 B.R. 827 (Bankr. W.D. Tex. 1991) (votes of insiders disqualified who had purchased claims to prevent the proponent of a competing plan from purchasing them, because such conduct constituted an "obstructionist tactic done in contemplation of gaining an unfair advantage over other creditors" and because "such conduct cannot, as a matter of law, be in good faith"); *In re Allegheny International*, 118 B.R. 282 (Bankr. W.D. Pa. 1990) (acquisition of a blocking position was in bad faith because it was aimed at defeating the debtor's plan and was meant to obstruct a fair and reasonable organization); *In re Holly Knoll Partnership*, 167 B.R. 381, 388 (Bankr. E.D. Pa. 1994) (finding that the purchasing creditor was not acting to protect or maximize its rights as a creditor but, rather, was acting to preserve financial advantages it would receive if the plan was confirmed, enabling it to gain control of the debtor and to collect certain management and construction fees, the Bankruptcy Court disallowed such creditor's vote as not being in good faith).

Here, Respondent ***has admitted*** that the purpose of its claims purchases was to ***block confirmation*** of Figter's proposed plan of reorganization. In doing so, Respondent hoped to gain a preferential advantage over the other creditors. This is precisely the kind of behavior which this Court found constituted bad faith in *Young*, *supra*, 324 U.S. at 210-211. Furthermore, Respondent did, in fact, intend to obtain more that its ratable share of the bankruptcy estate. Respondent had, as ulterior motives in purchasing the claims,

the intent to, among other things, (1) foreclose on and thereby garner the equity in Figter's real property for itself; and (2) hamper Figter's ability and incentive to continue the pending adversary proceeding against Respondent. Moreover, as discussed in the Petition, Respondent was not simply attempting to act in good faith to advance what it reasonably has determined to be its best interests as a creditor in this case. Respondent purchased claims ***outside*** the secured class to which it belonged. (Petition at 19-20). The Ninth Circuit Opinion, however, refused to apply the holding of this Court's decision in *Young*, *supra*, that a selfish purpose to ***obstruct a fair and feasible reorganization*** constitutes bad faith, resulting in denial of the right to vote on a plan. If this Court's precedent had been followed and applied by the Court of Appeals, a finding of bad faith should have been made.

The Ninth Circuit Opinion is also in conflict with precedents of this Court on the issue of whether Respondent, if the claims it purchased are not designated as nonvoting, should have been found entitled to only one vote with respect to the claims it purchased. As discussed in the Petition, in a variety of pre-Code contexts, the assignee or holder of multiple claims in the same class has only one vote for purposes of voting in a bankruptcy proceeding. (Petition at 24-25). In *Dewsnup v. Timm*, 502 U.S. 410, 419-420 (1992), this Court held that, unless there is a discussion to the contrary in the legislative history, the Code is not to be construed as intending "to effect a major change in pre-Code practice." The Court of Appeals, however, effected a "major change in pre-Code practice," by rejecting analogous bankruptcy precedent in the context of the predecessor statutes to Chapter 11 of the Code without any reference to any legislative history which might justify such a departure.

Because of these conflicts with precedents of this Court alone, the Petition should be granted. Under the totality of the circumstances in this case, Respondent did not act with

proper motive or in a proper manner in its claims purchases and otherwise acted in bad faith. In finding otherwise, the Court of Appeals and the courts below have ignored the dictates of this Court that they must have as an ***overriding*** goal, insuring the success of the reorganization. The decisions below jeopardize the successful reorganization of not only the Petitioner but all Chapter 11 debtors and are contrary to the teachings of this Court, the purposes of the Code and the intent of Congress. The Petition should be granted so that the Court may exercise its supervisory power to correct this departure from applicable precedent and legislative intent.

3. Respondent Is in Any Event Entitled to Only One Vote for Each of the Unsecured Claims Purchased.

Contrary to Respondent's argument, the plain language of Section 1126(c) of the Code does not give a creditor a right to vote multiple claims and does not bar any inquiry into pre-Code case law. The Petition (at 24-28) cited the historical rule, analogous pre-Code cases and excerpts from the *Colliers* treatises, all of which demonstrate that multiple purchased claims should be tallied as one vote. The language of the Section 12 of the Bankruptcy Act and Section 1126(c) are virtually identical. Section 1126(c) does *not* expressly address the issue of the voting of multiple purchased claims. Neither the statute nor the legislative history contains any reference to or discussion of this issue. Therefore, Section 1126(c) does not contain "plain language" which sufficiently expresses a clear intent to change pre-Code practice. A Court reviewing the issue must accordingly conduct an inquiry into pre-Code cases and Congressional intent.

The Petitioner and Respondent both cite *Dewsnup v. Timm*, *supra*, but for different propositions. Respondent

cites *Dewsnup* for the proposition that the language of Section 1126(c) is unambiguous and any judicial inquiry should end there. (Resp. Br. at 10). The Petitioner cites *Dewsnup* for the proposition that the Code was not written on a completely "clean slate," nor enacted in a statutory vacuum. 502 U.S. at 419-420 (Petition at 26-27). To interpret the Code in a vacuum is not only counter-intuitive, but it also flies in the face of a long line of jurisprudence which cautions the Courts against an approach which ignores precedent and the statutory frameworks which existed prior to the enactment of the Code. *Dewsnup* holds that, unless there is a discussion to the contrary in the legislative history, the Code is not to be construed as intending "to effect a major change in pre-Code practice." *Id. See also Pennsylvania Public Welfare Dept. v. Davenport*, 495 U.S. 552, 563 (1990) (the Code should not be read to abandon past bankruptcy practices absent a clear Congressional intent to do so).

Even though Section 1126(c) refers to allowed "claims," that Section simply does not attempt to address how claims should be counted in the context of claims trading or where a creditor buys multiple claims which, through the sale process, have lost any independent basis by being aggregated by one party. Despite this, the Courts below effected a "major change in pre-Code practice," without any reference to any legislative history which might justify such a departure. To be consistent with *Dewsnup*, there would have to be a much clearer indication of intent by Congress to abrogate the prior case law and statutory rules which governed voting in a variety of previous statutory contexts. (Petition at 27). The "plain language" rule simply cannot be applied to Section 1126(c), which is completely devoid of any language regarding vote counting of multiple purchased claims. The Courts below nevertheless adopted broad new rules of voting, simply on the basis of the use of the word "claims" in Section 1126(c), as opposed to the words "claimants" or "creditors." Under applicable precedents of this Court, this is not enough to effect a major change in pre-Code practice.

Therefore, the Petition for Writ of Certiorari should be granted to determine whether the Ninth Circuit correctly ignored and disregarded prior precedents, under predecessor statutes, in a variety of analogous contexts, in refusing to find that Respondent is only entitled to one vote by virtue of the multiple unsecured claims which it holds.

CONCLUSION

This Court should grant certiorari to determine as a matter of law whether the claims purchases at issue were in bad faith within the meaning of Section 1126(e) of the Code or, alternatively, to determine that a purchaser of claims under the Code should be entitled to only one vote as to the claims it purchased.

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Respectfully submitted,

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